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No. 18819

United States
Court of Appeals
for the Ninth Circuit

PHOENIX TITLE & TRUST COMPANY — Appellant

vs.

ARTHUR PEABODY AND
OLIVE PEABODY — Appellee

On Appeal from the United States District Court
for the District of Arizona

Brief for Appellant

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JURISDICTIONAL STATEMENT

This is an appeal from an Order on Review of the District Court of Arizona entered on March 29, 1963, sustaining the Findings of Fact I, II, III and IV and Conclusions of Law 1, 2, 3, 7, 8, 16 and 17 of the Referee in Bankruptcy dated May 31, 1962, and a Turnover Order of the same date.

The District Court had jurisdiction by virtue of a Petition for Review filed by the Appellant June 11, 1962 under the provisions of Title 11 Bankruptcy Sec. 11 a(10) United States Code and the Referree in Bankruptcy had jurisdiction by virtue of a Petition for Determination of Custody and Possession of Assets and for Turnover Order filed by Trustee in Bankruptcy of Arthur Peabody and Olive Peabody, husband and wife, dated August 18, 1960, and Petition for the Determina-

tion of Priority Among Creditors and Permission for Phoenix Title & Trust Company to Control Trust Property in Accordance With Trust Agreement Subject Only to Priority Rights of Creditors as Established by Referee filed September 23, 1960, under the provisions of Title 11 Bankruptcy Sec. 11 a(7) United States Code.

Pleadings which show the existence of jurisdiction are Petition for Involuntary Bankruptcy (TR 1), Petition for Determination of Custody and Possession of Assets and for Turnover Order (TR 63) and Petition for the Determination of Priority Among Creditors and Permission for Phoenix Title & Trust Company to Control Trust Property in Accordance With Trust Agreements Subject Only to Priority Rights of Creditors as Established by Referee (TR 66). The position of Phoenix Title was that it had title and right to possession of the assets in question, was an adverse claimant to the Trustee in Bankruptcy, but that the Referee in Bankruptcy had the right, power and jurisdiction to have a hearing to determine if he had jurisdiction over the specific assets in question. (RT 12-1-60 pg. 5, 27).

STATEMENT OF THE CASE

A. FACTUAL BACKGROUND

This is a proceedings to establish the validity of a security interest of Phoenix Title and Trust Company in and to specified property and to determine if, by virtue of the legal device used, the rights of Phoenix Title and Trust Company are prior to those of the Trustee in Bankruptcy.

Arthur Peabody and Olive Peabody, husband and wife, on July 26, 1956, executed and delivered to and with Phoenix Title and Trust Company, an Arizona

corporation, a Trust Deed, dated July 23, 1956, (22,30)* a Trust Agreement known as No. 6007, dated July 23, 1956, (30,32) a Note for $50,000.00 dated July 24, 1956, payable to Phoenix Title and Trust Company (31,32), and a Collateral Assignment of Beneficial Interest in Trust 6007 and other assets of the Peabodys as security for the payment of the $50,000.00 Note (31,32) all as one complete transaction.

Financial difficulties developed for the Peabodys as a result of loss of a contractor's license and the condemnation of a portion of a shopping center on the trust property, but by that time through the sale of various parts of the trust assets or the assets collaterally assigned, the principal balance of the Note had been reduced to $42,536.24, together with interest from October 1, 1957 (TR 48 & 62).

Phoenix Title, as Trustee, assumed responsibility in connection with the condemnation suit under written agreements and as a result a $22,200.00 judgment was obtained and the State of Arizona paid a total of $26,093.82 to settle this judgment (39). From the date of the State of Arizona taking possession of the condemned portion of the premises, namely, June 1, 1957, to date, Phoenix Title and Trust Company has been in exclusive possession of the trust property (TR 72).

On December 12, 1958, Phoenix Title and Trust Company filed a suit to foreclose their mortgage lien (Collateral Assignment of Beneficial Interest) and continued that action until enjoined from further proceedings by the District Court on January 28, 1960 (Rep. Tr. 1-28-60) (TR 184).

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* Numbers refer to pages in Reporter's Transcript of Proceedings of December 1, 1960.

A petition for involuntary bankruptcy was filed by other creditors (TR 1) and the Peabodys were adjudged bankrupt effective April 15, 1959 (TR 16).

A brief, chronological list of the events that affect the issues in this matter is as follows:

Exhibit	*Creditor*	*Lien*	*Date*	*Amount*
	Peabody had title on 7-22-56 and before[1] (Note)*			
1.	Midway Lumber Co.	Mechanics Lien	12-18-56[2]	$ 2,415.76+
2.	Phoenix Title	Trust Deed	7-31-56[3]	
3.	"	Trust Agreement	7-31-56[4]	
4.	"	Note	7-31-56[5]	$42,536.24+
5.	"	Collateral Assign-ment	7-31-56[6]	
6.	Tucson News-papers, Inc.	Judgment	2-18-57[7]	$ 1,000.00+
7.	Midway Lumber	Judgment	2-19-57[8]	
8.	Condemnation Action filed Feb. 28. 1957[9]			
9.	Luella Don	Judgment	4-26-57[10]	$ 1,250.00+
10.	Michael Melynkovich	Judgment	6-3-51[11]	$10,668.23+
11.	Midway Lumber	Lis Pendens	6-5-57[12]	

* Note all references are to Rep. Tran. 12-1-60

[1] Page 20, 21, 30, 33.
[2] Page 20, 21, 33.
[3] Page 22, 30.
[4] Page 30, 32.
[5] Page 31, 32.
[6] Page 31, 32.
[7] Page 34, 35.
[8] Page 35, 36.
[9] Page 36.
[10] Page 37.
[11] Page 37.
[12] Page 37.

Exhibit	*Creditor*	*Lien*	*Date*	*Amount*
12. & 13.	Johnson	Deed & Assignment, etc.	6-21-57[13]	
14.	Amer. Radiator & Standard Sanitary Corp.	Assignment condemnation proceeds and interest in trust	7-31-57[14]	$ 2,072.00+
15.	Midway Lumber	Assignment, etc.	7-31-57[15]	$ 1,158.03+
16.	A. R. Garrett	Assignment, etc.	7-31-57[16]	$ 1,108.68+
27.	United States	Tax Lien	8-28-57[17]	$ 4,268.21+
17.	Jack Henry	Judgment	9-7-57[18]	$ 2,027.31+
18.	Herman J. Goldstein	Judgment	9-17-57[19]	$ 575.00+
28.	United States	Tax Lien	9-21-57[20]	$ 2,076.67+
19.	Lohse, Donahue & Bloom	Attorney's Lien	10-31-57[21]	$ 3,625.50+
20.	Employment Security Commission of Arizona	Tax Lien	11-21-57[22]	$ 83.31
21.	Jackie C. Stewart	Judgment	12-3-57[23]	$ 3,685.40+

[13] Page 37, 38.
[14] Page 38.
[15] Page 38.
[16] Page 38, 39.
[17] Page 41.
[18] Page 39.
[19] Page 39.
[20] Page 41.
[21] Page 39.
[22] Page 39, 40.
[23] Page 40.

Exhibit	*Creditor*	*Lien*	*Date*	*Amount*
22.	Employee's Liability Assurance Co. Ltd.	Judgment	1-20-58[24]	$ 2,200.00+
23.	Builder's Mortgage & Trust Co.	Judgment	1-25-58[25]	$ 4,841.80+
24.	Builder's Mortgage & Trust Co.	Judgment	1-25-58[26]	$ 4,841.80+
25.	Edwin W. Smalley	Judgment	4-15-58[27]	$ 9,898.00+
26.	William T. Fitchett	Judgment	4-15-58[28]	$ 2,085.04+

Most of the creditors having secured a judgment against the Peabodys also have taken assignments of rights to the condemnation money and in some cases an actual assignment of the beneficial interest in trust of the Peabodys (38).

Notwithstanding the fact that record title to all assets was in Phoenix Title and Trust Company, no creditor ever claimed that he had made any investigation as to the terms and conditions of the trust, the ownership of the beneficial interest or any other point in connection therewith, it being conceded that no investigation was in fact made by anyone.

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[24] Page 40.
[25] Page 40.
[26] Page 40.
[27] Page 41.
[28] Page 41.

With reference to the money secured by the condemnation judgment, Lohse, Donahue & Bloom claim and allege an Attorney's Lien as the first claim. This position was sustained by the Referee and District Judge and is not under appeal. The superior position of Midway Lumber under their Mechanics Lien has also been resolved and will be paid by stipulation from the condemnation money.

On August 18, 1960, Myles C. Stewart, the Trustee in Bankruptcy, filed a Petition for Determination of Custody and Possession of Assets and for Turnover Order with reference to the condemnation proceeds (TR 63). Phoenix Title and Trust Company, without every submitting to the jurisdiction of the Bankruptcy Court, but at all times recognizing and stipulating that the Bankruptcy Court had jurisdiction to hold a hearing to determine if it had authority to sign a Turnover Order, on September 23, 1960, filed a petition with the Bankruptcy Court alleging rights to the condemnation proceeds and asking that its rights to these proceeds be established (refuse turnover order), that the trust continue in accordance with its terms, that the order of priority of creditors be established and that the Title Company be authorized to pay those creditors and the then balance, if any, be paid to the Trustee in Bankruptcy (TR 66).

At the pre-trial meeting, a stipulation admitted into evidence all exhibits indicated above, and it is from these documents that the rights of all parties are based (41,42). The key instruments in this case have several different exhibit designations at various times, but the following designations used for the greater part of the time refer to the same instruments:

	Pre-Trial		
Trust Deed	2	or	1
Trust Agreement	3	or	1B
Note	4	or	1C
Collateral Assignment	5	or	1D

Finding of Fact and Conclusions of Law and a Turnover Order were issued by the Referee in Bankruptcy May 31, 1962 (TR 123, 138, 158). The Trustee in Bankruptcy petitioned the District Court for Review as to Conclusions of Law 14 and 15 and for failure to decide an issue under Sec. 70 (c) of the Bankruptcy Act (TR 141). Phoenix Title and Trust Company petitioned with reference to Findings of Fact I, II, III, IV and Conclusions of Law 1, 2, 3, 7, 8 (9), (10), 11, 13, 16 and 17 and the Turnover Order (TR 143). The District Court, on March 29, 1963, reversed the Referee on Conclusions of Law 11 and 13 and sustained all other points (TR 171), ruling that this was a passive trust and therefore void, the Collateral Assignment is an unrecorded mortgage voidable under Sec. 70(c) of the Bankruptcy Act or that it was an unfiled mortgage of personal property void under Arizona law.

B. LEGAL BACKGROUND

Under Arizona law, Phoenix Title and Trust Company has a security interest in the nature of a mortgage on real property which the Trustee in Bankruptcy claims. The security interest claimed vested long before the 4 month period concerning preferential treatment to creditors commenced. Bankruptcy Act § 3(a)(2); 11 USCA § 21(a)(2); 11 FCA Title 11, § 21(a)(2). The validity of the lien of Phoenix Title and Trust Company is determined by Arizona law as distinct from Federal law.

SPECIFICATIONS OF ERRORS RELIED ON

The District Court erred in sustaining the Referee in Bankruptcy's Findings of Fact II, III, and IV (pages 125 and 126 of the (Record) and Conclusions of Law 1, 2, 3, 7, 8 (pages 132 and 133 of the Record) and 16 and 17 (page 135 of the Record) as a result of which findings of fact and conclusions of law the District Court:

1. Failed to construe the Trust Deed, Trust Agreement, Promissory Note and Collateral Assignment together as collectively constituting a security device in the nature of a mortgage.

2. Failed to construe the instruments listed in paragraph 1 together so that the active duties of the Trustee under the Collateral Assignment were disregarded and the trust found to be a passive trust executed by the Statute of Uses.

3. Erred in construing the Trust Deed and Trust Agreement as not creating an active trust even if the District Court was correct in failing to construe the Promissory Note and Collateral Assignment as part of the same transaction.

4. Erred in failing to apply the doctrine of *Barringer v. Lilly*, Cir 9, 96 F.2d 607, as it applies to the creation of a security devise and the giving of notice by the recorded Trust Deed thereby perfecting the lien of Phoenix Title and Trust Company against all subsequently recorded liens.

QUESTIONS PRESENTED

1. Whether it is necessary to construe all the documents mentioned in the Specification of Errors together in order

(a) To determine if the lien of Phoenix Title and and Trust is a valid recorded lien prior in time to the liens of all creditors of Arthur Peabody, except Midway Lumber Company; and

(b) To determine if the trust created was passive and thereby executed under the Statute of Uses.

2. Whether — if the documents mentioned in the Specifications of Errors need not be construed together — the trust created by the Trust Deed and Trust Agreement alone was passive and thereby executed under the Statute of Uses.

3. Whether — if the documents mentioned in the Specifications of Errors need not be construed together — the trust created by the Deed, Trust Agreement, and the Promissory Note and Collateral Assignment was not, because of the recorded Trust Deed, a valid lien prior in time to the liens of all creditors of Arthur Peabody except Midway Lumber Company notwithstanding the trust so created was a passive trust.

ARGUMENT

A. SUMMARY OF ARGUMENT

In effecting its lien against the property subject to this appeal, Phoenix Title and Trust Company caused four instruments to be executed by the bankrupts, Arthur Peabody and wife, all of which were executed on the same day, to-wit: July 26, 1956, as part of the same transaction and covering the same subject matter. The instruments executed that day constituting

the security of Phoenix Title and Trust Company for the advancement of $50,000.00 were collectively intended as a mortgage by the parties. The Trust Deed which was recorded constituted notice of the existence of a trust to all the world including possible bona fide purchasers and of the Trustee's power to make sales and conveyances. The Trust Agreement was the vehicle by which sales could be made of the trust property in order to provide the funding for the payment of the Promissory Note secured by the Collateral Assignment. The duties of the Trustee in enforcing the security created by this package of instruments were active duties, and the lien of Phoenix Title and Trust created thereby was, as of the date of the recording the Trust Deed, to-wit: July 31, 1956, good against all subsequent creditors under the doctrine of *Barringer v. Lilly*, 9 cir. 96 F.2d 607, in that any potential creditor of the bankrupts would be charged with knowledge of the terms of the Trust Deed and of the existence of the trust and if inquiry were pursued would have discovered the existence of the package constituting the terms of Phoenix Title and Trust Company's lien. Even if the instruments are not construed together and the Trust Deed and Trust Agreement are construed separately from the Collateral Assignment and Promissory Note secured thereby, the Trust Agreement is active by its terms and was in fact actively operated as of the date of bankruptcy. Finally, irrespective of any issue of active or passive trust, the lien of Phoenix Title and Trust Company was good as of July 31, 1956, against all subsequent creditors under the doctrine of *Barringer v. Lilly supra* in that record title was in Phoenix Title and Trust Company as Trustee, so that regardless of the legal efficacy of the other instruments concerned with the creation of

the lien, the record title in Phoenix Title and Trust Company as Trustee estops any potential bona fide creditor purchaser from assertitng a subsequently recorded lien.

B. NECESSITY TO CONSTRUE INSTRUMENTS CREATING LIEN TOGETHER

The critical instruments involved in this appeal are a Trust Deed (Exhibit 2), Trust Agreement (Exhibit 3), Promissory Note (Exhibit 4) and Collateral Assignment of Beneficial Interest (Exhibit 5). It is Appellant's position that these instruments all having been executed and delivered concurrently on July 26, 1956, collectively constituted the security for Phoenix Title and Trust Company's advance of $50,000.00 to Arthur Peabody the bankrupt. The general rule is that

> "where several instruments, executed contemporaneously or at different times pertain to the same transaction, they will be read together although they do not expressly refer to each other."
> Vol. 17A, C.J.S. Sec. 298, Separate writings, page 128. Restatement of Contracts 237C. *Clark v. Levy,* 25 Ariz. 541. 220 Pac. 232.

The foregoing is a rule of construction to determine the intent of the parties, and an examination of the documents Exhibits 2, 3, 4 and 5 show the Trust Deed was given and delivered and recorded to give notice to the world of the existence of the trust, a Collateral Assignment was given to secure the Note, and the Trust Agreement, which contained provisions providing for the sales of lots of the trust property, constituted the vehicle by which repayment of the Note and Collateral Assignment would be effected. The only purpose of the Trust Agreement was to act

as a vehicle for funding the repayment of the debt; that is obvious from its terms and the fact it was executed simultaneously with the other instruments. All four instruments should, consistent with the intentions of the parties, be regarded as part of the same transaction and construed together. By way of comparison it is notable that in *Barringer v. Lilly supra* the instruments consisted of a Trust Agreement in the nature of a Contract for the Sale of Real Estate in that one beneficiary was the seller and the other beneficiary was the buyer, a Promissory Note and a Trust Deed. If it were not for the existence of the Promissory Note in *Barringer v. Lilly* the Court undoubtedly would have determined the instruments executed were in the nature of a land purchase contract, but because of the existence of the Note, the Court held that the transaction was intended as a mortgage. Thus, the Court in *Barringer v. Lilly* in determining the nature of the transaction and the intention of the parties looked at all the instruments collectively and found

> "The fact that Tunney gave a Note for $85,000.00 and that the declaration of trust recited that it was to secure payment of the Note seemed to lead irresistibly to the conclusion that the declaration of trust was regarded as a mortgage."

The instruments used in the Peabody case were the same Trust Deed as used in *Barringer v. Lilly*, the same Promissory Note, but a declaration of trust was employed to provide for lot sales as a means of funding the repayment of the Note; the Collateral Assignment is substantially the same as the usual Mortgage in this jurisdiction so that the instruments in the instant case are more conventional as establishing a mortgage than those of *Barringer v. Lilly* where the

declaration of trust was a hybrid between a Mortgage and a Contract for the Sale of Real Estate. Accordingly, it follows that if all the instruments executed in the instant case are treated as part of the same transaction and as constituting a mortgage, the facts of this case come squarely within the rule of *Barringer v. Lilly,* wherein the Court in speaking of Sec. 969 of the Revised Code of Arizona 1928 (now 33-412(A), Arizona Revised Statutes) said:

> "This statute protects creditors and innocent purchasers against an unscrupulous or dishonest *owner of record in possession* . . . if inquiry was made by the creditors they would have actual notice of the declaration of trust else how could Owens explain away the record title in the title and trust company.
>
> "It being established that record title was in the title and trust company, it follows that all creditors were creditors with notice of the fact that Owens and his associates were not owners of the tract, at least so far as the record was concerned — which is notice to all the world."
>
> 9 Cir 96 F.2d 607 at 612-613.

Again the Court, at page 613 states:

> "In either case, the record title in the Title and Trust Company would be sufficient to put all persons on notice that Owens, Denmore and Mills did not own the property or that it was encumbered. Such a deed would then be a conveyance in the nature of a mortgage with the title in one person subject to being defeated by the performance of a condition."

It is interesting to note in the quoted portion immediately above that the Court in *Barringer v. Lilly construed the deed as constituting a mortgage* and looked to the other instruments for the establishment of the

condition the performance of which would defeat the title in the record holder. In any event, the Court construing the deed as the mortgage established the principle that the recording of the deed satisfied the recording statutes of Arizona. The above rule enunciated by the Court that the deed constituted the mortgage, even though it was a Trust Deed, is comparable to the established rule in Arizona that a deed absolute on its face given as security for a debt constituted a mortgage. *Coffin v. Green*, 21 Ariz. 54, 185 P. 361. *Rogers v. Greer,* 70 Ariz. 264, 219 P.2d 760.

The ruling of the District Court on March 29, 1963 (TR 171), can have no application if the instruments, Exhibits 2, 3, 4 and 5 are construed together to form the mortgage insofar as that ruling affirms the Referee in Bankruptcy in determining that the trust created was a passive trust, because if the instruments collectively constitute a mortgage, the duties of the Trustee in enforcing the terms of the mortgage are absolute duties which in the event of a default impose a mandatory duty of foreclosure. There can be no dispute that if the Trustee is deemed to have duties under the Collateral Assignment provisions of the trust arrangement, that the duties are active in the full sense of the phrase and the trust is not executed by the Statute of Uses.

C. WHERE TRUST INSTRUMENTS ARE NOT CONSTRUED TOGETHER

(1) Appellant's Position

Even if the trust instruments are not construed together, and the Trust Deed and the Trust Agreement, Exhibits 2 and 3 respectively, are construed together disregarding fully, however, the Note and Collateral Assignment, it is the position of Phoe-

nix Title and Trust Company that the Trust Deed and Trust Agreement by their terms establish active duties removing the trust from the operations of the Statute of Uses. If these two instruments create active duties effecting an equitable conversion so that the rights of the beneficiary, Peabody, are personal property, then these rights are subject to assignment for security purposes by a Collateral Assignment beyond the purview of the Arizona real property mortgage recording act (Sec. 33-412A, Arizona Revised Statutes). Under the California cases, the Trust Agreement and Trust Deed create a trust, the terms of which cannot be carried out unless the beneficiaries' interests are mere contract rights. Thus, the California Supreme Court in *Craven v. Domequez Estate*, 237 Pac. 821 at 824, stated:

> "The title insurance and trust company as trustee, therefore took an estate in the trust property adequate to the execution of the trust and as the trust was to convey an absolute title to the lands and to distribute the proceeds of all sales thereof, it was necessary for it to own and hold the absolute title to the trust property. This was clearly provided for in the instruments executed by the parties and created the trust."

And in *Wright et al. v. Security First National Bank of Los Angeles*, 95 P.2d 194, the contention was made that a subdivision land trust would not convert the beneficiaries' interest into personal property unless it were mandatory under the trust agreement for the trustees to sell all the real property in any event, and there must be no power of termination of the trust or contingency upon which any part of the land could be returned to the grantor. The Court rejected this contention, stating at page 198:

> "In Smith vs. Bank of America etc Association supra the trust agreement provided that the trust might be closed by the conveyance of any unsold portions of the property to the beneficiaries, but it further provided that the interest of each beneficiary was personal property and not an interest in the property conveyed to the trust. Although the interest of the creditor was being considered it was held that the beneficiaries had no interest in the real property."

An examination of the Smith case — *Smith v. Bank of America National Trust & Savings Assoc.*, 57 P.2d 1363 — will show that the California Supreme Court considered the importance of the language of the trust agreement providing the beneficiaries' interest would be personal property as well as the fact that the trustee might reconvey to the benefciary any unsold real property. Thus the Court stated at page 1367:

> "While it is true that words in a trust agreement to this effect do not create a conversion of real property to personal property, it throws some light on the intention of the parties to the trust agreement, as stated the intention is the criterion. Keeping this in mind, we may go to the trust agreement itself to find what burden is cast upon the trustee . . . It provides that the trustee holds the title in trust (1) to sell and convey the property; (2) to release from the lien of the indebtedness secured by it any and all lots; (3) to receive and disburse the moneys received from the sale of lots . . . (4) to sell the beneficial interest created by the trust agreement as may be necessary to satisfy defaults and reasonable expenses and trust agreements (5) and to publish the required notices therefor (6) and may close the trust 'by the sale of all property hereunder; provided, however, that in the event said trust should be closed by conveyance of said property or any

remaining unsold portions thereof to the beneficiaries or their nominees without consideration' . . ."

Comparing the Peabody Trust Agreement to the Smith agreement, following are its material provisions:

(1) "Purposes of *subdividing, platting, deeding, selling, conveying, receiving payment* . . . Trustee is . . . granted full power to do all acts necessary to accomplish the purposes . . ." ART. I. The foregoing were to be carried out by the Trustee at the beneficiaries' direction. (emphasis supplied)

(2) ". . . it is further agreed the Trustee is authorized *to dedicate* to the public use all road, alley . . . necessary for . . . The trustee is . . . authorized to . . . record . . . restrictions." ART. II (emphasis supplied)

(3) ". . . the trustee shall have the right to include the property held hereunder in the . . . Liability Policy carried by Phoenix Title and Trust Company." ART. III.

(4) All instruments . . . shall be *executed solely by* . . . Phoenix Title . . . Any *sales agreements* executed by the trustee . . ." ART. IV (emphasis supplied)

(5) ". . . all funds . . . from leasing or sale . . . *shall be paid to the trustee and thereafter disbursed by the Trustee as follows*: . . ." ART. V (emphasis supplied)

(6) ARTICLE VI provides for title policies and ARTICLE VII for accounting and "The beneficiaries shall be entitled to *monthly statements* from the Trustee . . ." ART. VII (emphasis supplied)

(7) ARTICLE IX provides *no one required to look to trustee's authority to act* and ARTICLE X provides:

"The interest of the beneficiaries in this trust is *personal* property, and the beneficiaries have not and *shall not at any time have any right, title, or interest in* . . . the property . . ., and have not and *shall not have any* . . . power *to . . . secure dissolution or termination of this trust or the partition* . . . The sole right . . . of the beneficiaries is to enforce the . . . terms of this trust . . ." ART. X (emphasis supplied)

(8) "*No assignment . . . shall be valid* . . . until . . . accepted by the trustee." ART. XII (emphasis supplied)

(9) ARTICLE XIV provides for termination of the trust on

"Conveyance of all the property by the trustee . . ., and the distribution of all the funds . . . In the event said property has not been conveyed by . . . *July 23, 1961*, the trustee *may* . . . convey the property to the Beneficiaries, and the trust shall be . . . terminated." (emphasis supplied)

In addition, the Trust Deed itself, Exhibit 2, granted the Trustee the following powers of record:

To hold, sell and convey, mortgage or pledge the trust property, to handle the said property in the same manner as though Phoenix Title and Trust Company had the property in fee simple and not as trustee. The power to plat into blocks, lots, tracts, etc., and to dedicate portions thereof as parks, streets, etc., full power to

"sell and convey the property hereby conveyed and hereafter described on such terms as the said trustee shall designate, to make, execute and deliver deeds therefor and to do all further acts . . . for the carrying out of the above purposes."

Accordingly the Peabody trust, among the beneficial duties of the Trustee, required the Trustee to *sell, execute sales agreements, and convey,* as well as numerous other duties concerning subdividing, platting, etc., and there was the duty to accept assignments of the beneficial interest. Among the protective or administrative duties of the Trustee the trust required the Trustee to make accountings, render monthly statements, receive and disburse funds, and keep the property insured for public liability. These duties go way beyond the two affirmative duties required to make a trust active under *Restatement of Trusts,* Sec. 69.

Above all, the trust was irrevocable (Article X of the Trust Agreement, Exhibit 3) until all the property was sold or until July 23, 1961, if not sold, but even in the latter case the language of the trust actually does not require the Trustee to reconvey the remaining land(although after July 23, 1961, the trust would become passive). The beneficiaries could not get the property back (Article X) since they are prohibited from partitioning or dissolving prior to July 23, 1961. *Breen v. Breen,* 103 N.E.2d 625 at page 627.

The trust is an active, irrevocable trust for a definite term imposing on the Trustee many duties but especially the *duty to convey,* and the interest of the beneficiaries is by the terms of the Trust Agreement declared to be personal property.

It is therefore clear that equitable conversion has resulted:

> *Restatement of Trusts,* § 131 Equitable Conversion.
>
> "(1) If real property is held in trust and by the terms of the trust a duty is imposed upon the trustee to sell it and hold the proceeds in trust or dis-

> tribute the proceeds, the interest of the beneficiary is personal property."

Since the *Restatement* is the law in Arizona by which the Peabody Trust Agreement's legal effect is determined —

> "We have repeatedly stated that where not bound by previous decisions of this court or legislative enactment we will follow the Restatement of Law." *Ingalls v. Neidlinger,* 216 P.2d 837, 70 Ariz. 40; *Bristor v. Cheatham,* 255 P.2d 173, 75 Ariz. 277; *Waddell v. White,* 109 P.2d 843, 56 Ariz. 525; *Rodriquez v. Terry,* 290 P.2d 173, 75 Ariz. 277 —

it is clear that the interest of the Peabodys was personal property at the time they executed the Collateral Assignment. And

> "The Statute of Uses does not execute a use or trust created upon any interest except a freehold interest in land." *Restatement of Trusts,* Sec. 70

If it is contended that because the Peabodys might eventually get the real property back equitable conversion did not occur, the Illinois Supreme Court has answered that contention as follows:

> The rule has been long and well established in this State that the form of Deed of Trust and Trust Agreement before us created a valid and subsisting trust under which the interest of the beneficiary is personal property only and not real estate. It has been repeatedly held that an agreement creating an interest in the profits or proceeds of the sale of real estate creates no interest in or lien upon the land itself. . . . It is true that under the terms of the Land Trust Agreement, Shrader, the beneficiary, had the power to direct the trustee to convey the real estate to him and thus reconvert his interests in said land trust into real estate, but until he exercised such power his in-

> terest remains personalty so long as the trust continues in effect and before such reconversion is actually accomplished."
>
> *Chicago Title and Trust Co. v. Mercantile Trust & Savings Bank.* 20 N.E.2d 992 at 995.

Continuing on page 996 the Court said:

> "It follows that the interest of Shrader, the beneficiary of the Land Trusts, being personal property, the Statute of Uses did not operate to reconvert or change the character of the estate of such beneficary from personal property to real estate. That requred an election or exercise of power by the beneficiary himself. The Statute of Uses does not operate upon personal property interests but only upon interest in real estate."

Further, if it is contended that the duties of the trust company are ministerial under the Peabody Trust Agreement, such is not significant. What is important is that there be affirmative duties, and it matters not that the Trustee's duties don't arise until the beneficiary gives an order. Thus in *Chicago Title v. Mercantile Trust supra* at page 996 the Court states:

> "Even though we assume that Shrader, the beneficiary, had the equitable title to the land, would the Statute of Uses execute the trust? The Statute would not operate because the trustee has active duties to perform under the trust agreement sufficient to remove the trust from the class which the Statute of Uses executes. Although it is repeatedly asserted in appellant's brief that the trust under consideration is one that is dry and passive because the trustee has no duties to perform, it is expressly covenanted in the trust agreement that the trustee will at the written direction of Shrader 'make deeds for, or otherwise deal with the title to said real estate' and that 'if any property remains in the trust twenty years from this

> date it shall be sold at public sale by the trustee on reasonable notice, and the proceeds of the sale shall be divided among those who are entitled thereto under this agreement'."

And:

> "If active duties are imposed it does not matter that they are merely formal or ministerial."
>
> *Gordon v. Baxter*, 127 N.E. 717, 293 Ill. 547.

Finally, it should also be noted that the Peabody Trust Agreement has a maximum 5 year term: 7/23/56 - 7/23/61, and it is universally held that:

> "c. Equitable non-freehold interest.
> Although the property held in trust by the trustee is real property, the interest of the beneficiary is personal property if it so limited in duration that it is a non-freehold interest."
>
> *Restatement of Trusts*, Sec. 130, Comment C, 90 C.J.S. Trusts, Sec. 186, p. 79.
>
> *DeHaven v. Sherman*, 22 N.E. 711, 131 Ill. 115.

(2) Authorities Cited by the District Court.

(a) The District Court's decision of March 29, 1963 (page 171 of the Record), cites *Janura v. Fancl*, 52 N.W.2d 144, and *Gallagher v. Drovers Trust & Savings Bank et al.*, 88 N.E.2d 870, in support of the proposition that the Peabody Trust, as reflected by the Deed and Trust Agreement only, Exhibits 2 and 3, is a passive trust. Both these cases involved actions for partition and in no way involved transfers for security purposes or subdivision land trusts. In *Janura* the court stated at page 145

> "The trust instrument also recited that the beneficiaries should have the management and control of the property and of the selling, vesting and han-

> dling thereof, and that the trustee would have *no duties* to perform for twenty years." (emphasis supplied)

The trust instrument in this case by its terms was inactive for the 20 year period, so that partition when sought was inevitable. Not so the Peabody trust where the Trustee had the active duties previously outlined and had, in fact, exercised those duties under the Trust Deed and Trust Agreement by making sales reducing the Note (Exhibit 4) from $50,000.00 to $42,000.00 (see paragraph 2 of Statement of the Case).

In the *Gallagher case*, in granting partition the Court stated:

> "In affirming a decree awarding partition the court held that an equitable conversion is not effected where a trust agreement attempts to create an equitable conversion but provides no definite time for the sale of the land and makes no specific provsion for termination of the trust."
>
> 88 N.E.2d 870, 873.

The Peabody trust by its own terms was terminable on July 23, 1961. (ARTICLE XIV of Exhibit 3).

(b) *Chattel Mortgage Recording Provisions Cited by the District Court.*

In the District Court's order of March 29, 1963 (TR 171), the Court declared that if the interest of the Peabodys was personal property the assignment of that interest was invalid because of failure to comply with the Chattel Mortgage recording statutes of Arizona.

The District Court in this decision ignores the notice effect of recording the Trust Deed, as announced in *Barringer v. Lilly, supra.*

However, irrespective of the notice effect of the recorded Trust Deed, an examination of the Chattel Mortgage recording statutes shows that the Arizona Chattel Mortgage recording statutes should not be construed to cover the mortgaging of intangibles. Article 4 of Chapter 6 of Arizona Revised Statutes is entitled "Chattel Mortgages" which, while not part of the statutes of Arizona, indicate the intention of the codifiers to provide mortgage procedures for tangibles (chattels). Sec. 33-751 Arizona Revised Statutes was adopted from West's Annotated Civil Code of California Sec. 2955, which provides as follows:

> "§ 2955 *Mortgageable Property*
>
> Mortgages may be made upon all growing crops, including grapes and fruit, and upon any and all kinds of personal property, except the following:
>
> 1. *Personal property not capable of manual delivery;*
> 2. Articles of wearing apparel and personal adornment;
> 3. The stock in trade of a merchant.
>
> Provided, however, that any nonprofit cooperative association with or without capital stock is not to be deemed a merchant within the meaning of this section." (emphasis supplied)
>
> West's Annotated California Codes Vol. 11, p. 266.

The italicized portions of the above statute were omitted when adopted by Arizona. Unless the omitted portion of the California statute is read into the Arizona statute, it follows that all transactions involving choses in action such as the pledging and escrow of stocks, bonds, and accounts receivable, are violative of the present Arizona statutes. Logically a Chattel Mortgage recording statute which is predicated on the

mortgaged chattel remaining in the possession of the debtor cannot be interpreted to cover intangibles. Security devices should be consistent with the kind of property to which the security attaches, which may or not (e.g. pledge) require the recording of a legal instrument. Though the statutory definition of personal property in Arizona includes intangibles, the chattel mortgaging statute should not be literally construed to void customary security devices involving intangibles, such as escrows, pledges, etc., whch do not require recording, nor should it be applied in this case where the intangible property is in the hands of the mortgagee.

(3) The Effect of Record Title in Phoenix Title and Trust Company.

It is Appellant's position that even if the Statute of Uses were deemed applicable and even if the Trust Deed, Trust Agreement, Note, and Collateral Assignment are not construed together, recording statutes are intended to protect bona fide purchasers and if the lien of Phoenix Title and Trust Company is valid against bona fide purchasers, it is valid for purposes of determining its lien under the Bankruptcy Act. Thus, in *Barringer v. Lilly,* the Court on page 614 stated:

> "We have already shown that the creditors are not creditors without notice and even though the declaration of trust may be void as to them there is no explaining away the record title in the name of Appellant title and trust company."

Thus, in *David v. Kliendienst,* 64 Ariz. 251 at page 258, 169 Pac. 2d 78, the Court stated:

> "The law seems to be settled that a person who fails to exercise due diligence to avail himself of information which is within his reach is not a

> bona fide purchaser. . . . Thus a purchaser who has brought to his attention circumstances which should have put him on inquiry which if pursued with due diligence would have led to knowledge of an adverse interest in the property is not a bona fide purchaser."

And in *Barringer v. Lilly*, 96 Fed. 2d 607 at page 613,

> ". . . The record title in the title and trust company would be sufficient to put all persons on notice that Owens, Denmore and Mills did not own the property or that it was encumbered."

In *Maricopa Utilities Company v. Kline*, 60 Ariz. 209 at page 214; 134 P.2d 156, the Court stated:

> "Notice of facts and circumstances which would put a man of ordinary prudence and intelligence on inquiry is equivalent to knowledge of all of the facts a reasonable diligent inquiry would disclose."

And:

> "Notice of the existence of a trust is by all the authorities held to impose the duty of inquiry as to its character and limitations and whatever is sufficient to put a person of ordinary prudence upon inquiry is constructive notice of everything to which the inquiry might have led."

Shaw v. Spencer, 100 Mass. 382 at 389.

The transcript is vacant of any evidence of any creditor of the bankrupt Arthur Peabody making inquiry of the trust of which notice existed pursuant to the recorded Trust Deed. Regardless of the application of the doctrines of the Statute of Uses, the construction of the trust instruments without reference to the Note and Collateral Assignment, the recording of the Trust Deed cannot be held to be an idle act, for

as the Court said in *Barringer v. Lilly,* 96 Fed. 2d 607 at page 612,

> "To hold as appellee Lilly urges that the record title of the title and trust company was meaningless would be to place land owners everywhere at the mercy of their tenants."

That the recording of the Trust Deed alone was sufficient record notice of Phoenix Title and Trust's lien is evident in the Arizona statute defining mortgages where a transfer in trust for security purposes is excepted:

> "§ 33-702 Mortgage defined; pledge distinguished, admissibility of proof that transfer is a mortgage.
>
> Every transfer of an interest in property, *other than in trust,* made only as a security for the performance of another act is a mortgage, except . . ." (emphasis supplied)

CONCLUSION

In view of the authorities, facts and argument set forth above, Appellant submits (1) that the District Court erred in not construing the trust instruments Exhibits 2, 3, 4 and 5 together as constituting a valid mortgage under the doctrine of *Barringer v. Lilly, supra;* (2) alternatively that the District Court erred in not finding the Trust Deed and Trust Agreement (Exhibits 2 and 3) created an active trust; and (3) alternatively that the District Court erred in disregarding the legal effect of the recording of the Trust Deed (Exhibit 2) as set forth in *Barringer v. Lilly, supra.*

Respectfully submitted,

LOHSE, DONAHUE & BLOOM

By .....
Attorneys for Appellant

I certify that, in connection with the preparation of this Brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing Brief is in full compliance with those rules.

Ashby I. Lohse
Attorney for Appellant

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

MYLES STEWART, Trustee of the Estate of ARTHUR PEABODY and OLIVE PEABODY,

Appellants,

vs.

PHOENIX TITLE & TRUST COMPANY,

Appellee.

No. 18819

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF ARIZONA

BRIEF FOR APPELLANTS

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JURISDICTIONAL STATEMENT

This is an appeal from an Order entered on March 29, 1963, by the United States District Court for the District of Arizona affirming the Order of the Referee in Bankruptcy entered May 31, 1962.

This appeal is brought under the jurisdiction established in Section 24 of the Bankruptcy Act, 11 USCA Paragraph 47.

INTRODUCTION

For the sake of clarity, the Phoenix Title & Trust Company, Inc., in its capacity as a creditor of the bankrupt estate will hereinafter be referred to as the "cred-

itor"; the Phoenix Title & Trust Company, Inc., in its capacity as Trustee under the terms of the conveyance by the bankrupts will hereinafter be referred to as the "Trust Company"; all events transpired in Tucson, Pima County, Arizona.

The Transcript of Record will be designated "T.R.", and the Reporter's Transcript will be designated "R.T."

STATEMENT OF THE CASE

This appeal is presented upon the theory that if a party desires any change in a judgment it must appeal. *Fidalgo Island Packing Company v. Phillips,* (9th Cir.) 253 F.2d 621 (1957).

The Trustee-Appellant agrees completely with the result of ruling of the United States District Judge and his reasons therefor. The District Judge did not sustain the portions of the Referee's Order which held that the Appellee's liens were inchoate as against liens of the United States, and that therefore, any rights which the Appellee, the "creditor," might have were voidable under Federal law by the United States and a Trustee in Bankruptcy under Section 70(e) of the Bankruptcy Act. These additional grounds in support of the ruling of the District Judge are the basis of this appeal.

The basic theory of the Referee and the United States District Judge in determining that the rights of Phoenix Title & Trust were void as to subsequent creditors was because the instruments creating a lien were unrecorded or unfiled in accordance with the Arizona statutes.

The appeal is presented to attempt to clarify the rights of creditors and to determine further the issue:

what is an inchoate lien as against liens for Federal taxes, and further, to give additional grounds for support of the ruling of the District Judge.

FACTS OF THIS CASE

That an involuntary Bankruptcy Petition was filed against the bankrupt Peabodys on the 15th day of April, 1959. That the Peabodys were duly adjudicated bankrupt. That the involuntary petition was filed by Ashby Lohse as attorney for William T. Fitchett, Edwin W. Smalley, and Paul E. Greer.

That prior to the filing and adjudication in the involuntary proceeding, the bankrupts and the Trust Company, the Appellee, entered into a transaction described as follows:

> By a recorded Deed, Exhibit 1, Recorder's Transcript, page 136, title to a parcel of real property in Pima County, Arizona, was transferred to the Trust Company, as Trustee. By a separate unrecorded Trust Agreement, Exhibit 1B, the title was held in trust for the Peabodys. The Trustee's Deed was dated July 23, 1956, and acknowledged by the Peabodys on July 26, 1956, was recorded at the request of the Trust Company on July 31, 1956, and duly appears in the records of the County Recorder, Pima County, Arizona. The beneficiaries of the trust are not named in the Trustee's Deed. The Trust Agreement, Exhibit 1B, dated July 23, 1956, was acknowledged by the Peabodys on July 26, 1956, and by officers of the Trust Company on July 31, 1956. Both the Trustees' Deed and the Trust Agreement bear the identification number, "Trust No. 6007."

The Trust Agreement provides that the property to which the Trust Company received title as Trustee (the real property described in the Trustee's Deed, Exhibit 1, which will hereinafter be referred to as the real property), was to be held in trust by the Trustee, the Trust Company, for the beneficiaries, Arthur Peabody and Olive C. Peabody, for the purposes of,

> "subdividing, platting, deeding, selling, conveying, receiving payment for and otherwise handling the property as a whole or in lots and parcels, upon such terms and conditions and for such prices as the Trustee may be instructed in writing so to do by the beneficiaries or their authorized representatives."

Under the provisions of the Trust Agreement, Exhibit 1B, the Trust Company is granted no discretionary powers and is charged with no responsibility in handling and managing the property. The prescribed duties of the Trust Company are ministerial in nature, to be performed under the direction of the beneficiaries. The settlors, Arthur Peabody and Olive C. Peabody, remained in possession and control of the property and were in possession and control of the property at the time of the bankruptcy herein, with all powers of management, charged with full responsibility for handling the property in carrying out the stated purposes of the trust.

The Trustee's Deed and the Trust Agreement contain no provision that the instruments were executed as security for the performance on the part of the Peabodys of any contract between them and the creditor. There is no reference in the Trustee's Deed or in the Trust Agreement to any other instrument executed or to be executed by the Peabodys as security for the performance on the part of the Peabodys of any contract between them and the creditor.

The Deed to the Trust Company as Trustee and the Trust Agreement were executed by the parties with the intention of establishing a passive depository of the legal title to the real property, with the actual and equitable ownership remaining in the Peabodys for their own use and benefit. The Trust Company as Trustee did not take title to the property as security for the performance of any contract or obligation to be performed on the part of the Peabodys.

On July 24, 1956, the Peabodys made their promissory note, Exhibit 1D, in the principal amount of $50,000.00, payable to the "creditor" on or before July 24, 1957, with interest at the rate of six (6%) per cent per annum from July 24, 1956, interest payable at maturity. The note recites that it is secured by a collateral assignment, Exhibit 1C, of Peabodys' beneficial interest in Trust No. 6007.

That the "creditor" drew checks payable as follows:

1. Check No. 108, in the amount of $32,701.45, to Arthur Peabody and Olive C. Peabody; for "proceeds of your loan from Phoenix Title & Trust Co."

2. Check No. 107, in the amount of $375.00, to Associated Engineering Co.; for "balance due for cross-sectioning streets in Littletown."

3. Check No. 106, in the amount of $16,712.31, to Valley National Bank; for "payment in full of mortgages from Ackley, DeBand, Kemmeries."

With their note given to the "creditor" on July 24, 1956, the Peabodys, as assignors, executed an instrument designated as "Collateral Assignment of Ben-

eficial Interest" (hereinafter referred to as the assignment) wherein the "creditor" is named as assignee. The assignment bears undated endorsements signed by officers of the "creditor," whereby the "creditor" approves and accepts the assignment as assignee and accepts the assignment as Trustee. The assignment was acknowledged by the Peabodys on July 26, 1956, but was never recorded.

That the Exhibits 1 (deed), 1B (Trust Agreement), 1C (Collateral Assignment), and 1D (note) do not constitute an assignment passing legal title to the "creditor," nor a present assignment of a beneficial interest in property. Furthermore, Exhibit 1C is not a mortgage.

The Collateral Assignment refers to the promissory note for $50,000.00, given by the Peabodys to the "creditor" on July 24, 1956, and provides that for the purpose of securing payment of said note, the assignor does thereby assign, convey, transfer and set over unto the assignee all of his rights, powers, privileges, proceeds and avails of the beneficiary created or reserved, and all of the interest of the beneficiary in Trust No. 6007, insofar as the real property is concerned. The "assignment" contains release clauses in relation to said property, reading as follows:

> "It is provided that the lots into which the property is subdivided may be released by assignor upon the payment to trustee for the benefit of assignee of the sum of $600.00 per lot, said amount to be applied first to the payment of interest to the first of the month next succeeding the date when such funds are available for distribution to assignee and the balance to be applied on (the) principal.
>
> "It is further provided that in the event that the

assignor herein has set up a sales escrow in the Phoenix Title and Trust Company that trustee will be authorized to convey a lot or lots to said assignor without the payment of any consideration provided assignor is obtaining a construction loan (including any refinancing, reneweal, or increase thereof) from a bona fide lending agency and provided said escrow provides that out of the sales price of said home the escrow agent shall remit the release price and all expenses of sale and conveyance by trustee for such lot or lots to the trustee, it being understood that this amount must be paid not later than the date on or before which the note secured hereby is to be paid in full. The release price herein referred to is the amount of $600.00 per lot as herein set forth."

The "assignment" also provides in the event of default on the part of the Peabodys in the payment of their note or any of the terms of the assignment that

> "the whole amount of the principal sum and any amount advanced by the assignee . . . shall be . . . deemed to have become due and the same . . . shall be collectible in a suit at law or by foreclosure . . . *as if this collateral assignment of Beneficial Interest were a mortgage. . . .*"
> (Emphasis supplied)

The assignment further provides for the appointment of a receiver "to take charge of said Beneficial Interest and said property."

A notice of tax lien against the Peabodys in favor of the United States of America, dated August 27, 1957, for $4,268.21, was filed August 28, 1957, fee No. 52633, in the office of the County Recorder of Pima County, Arizona.

A notice of tax lien against the Peabodys in favor of the United States of America, dated September 19,

1957, for $2,076.67, was filed September 21, 1957, fee No. 57827, in the office of the County Recorder of Pima County, Arizona.

The only documents recorded or filed in the office of the Pima County Recorder, or elsewhere in Arizona, as evidence of the agreement between the bankrupt and Phoenix Title & Trust Company, as Trustee, or Phoenix Title & Trust Company, the "creditor," was the Deed mentioned as Exhibit 1.

On December 12, 1958, the "creditor" brought an action against the Peabodys and others alleging, in substance, that the Peabodys had given the "creditor" their note for $50,000.00 on July 24, 1956, and in anticipation thereof, and as part of the same transaction, in order to secure the payment of said note, the parties made and executed the Trust Agreement wherein the Peabodys were beneficiaries and the Trust Company was Trustee under Trust No. 6007; that with the delivery of said note as part of the same transaction, in order to secure the payment of said note, the Peabodys executed and delivered to the "creditor" the assignment of all their beneficial interest in and to all the assets held by the Trust Company under Trust No. 6007; that the Peabodys had defaulted upon the note and assignment under the Trust securing said note; that the sum of $42,536.24, with interest from October 1, 1957, was then due. The complaint demanded, among other things, the following relief:

> "For judgment against Arthur Peabody and Olive C. Peabody, husband and wife, and Paul E. Green and Evelyn C. Green, in the sum of $42,536.24 together with interest as provided in said note from October 1, 1957, until paid for plaintiff's attorney fees in a sum equal to ten (10) per cent of all sums found due to date of judgment.

"That the respective *collateral assignments* of defendant Arthur Peabody's and Olive C. Peabody's beneficial interest in the assets of the trust hereinabove referred to be declared to be a first and prior lien against their interest in the property involved, and that said assignments be foreclosed as a mortgage, and the premises therein described and all of said defendants' interest under the terms of said trusts be sold under execution according to the law and practice of this Court to satisfy the demand of the plaintiff. That out of the proceeds of said sale, the plaintiff be paid the amount due; that in case of a deficiency arising from said sale, the plaintiff have judgment for the amount thereof; and that at said sale the plaintiff or any other person to this cause may become purchasers of said premises; that all defendants and all persons or corporations claiming to, under or from them and all persons having a lien subsequent to said Assignments be forever barred and foreclosed of and from all equity of redemption and claim of, in or to said assigned premises and every part and parcel thereof from and after the delivery of the Sheriff's Deed." (Emphasis supplied)

The action, designated in the docket of said Superior Court as No. 57402, had not been prosecuted to judgment at the time of bankruptcy herein and the case is still pending.

STATUTES INVOLVED

Arizona Revised Statutes:

Section 1-215, subdivision 22
Section 33-412A
Section 33-702
Section 33-751
Section 33-753, subdivision 5

Internal Revenue Code of 1954:

Section 6323

United States Bankruptcy Act:
Section 70(c)
Section 70(e)

SPECIFICATION OF ERRORS RELIED UPON

The District Court correctly sustained the Referee's ruling based upon certain of the premises expounded by the Appellant and affirmed by the Referee. However, the District Court erred in not concurring with the conclusion of law set forth in paragraphs XI and XIII of the Referee's Findings of Fact and Conclusions of Law. These conclusions found that under Federal law the lien of Phoenix Title & Trust, the "creditor," upon the property rights of the bankrupts was inchoate as against liens of the United States, and that the "transfer" by assignment is a "transfer" as defined by the Bankruptcy Act, which is voidable by the Trustee under Section 70(e) of the Bankruptcy Act.

QUESTIONS PRESENTED

1. Is an unrecorded mortgage of real property or an unfiled mortgage of personal property inchoate as to a subsequently recorded tax lien of the United States of America, that attached prior to the time of the filing of a Bankruptcy Petition?

2. Is an assignment, which is an inchoate lien, whether of an interest in real or personal property, voidable under Federal law and therefore null and void as against the Trustee in Bankruptcy under Section 70(e) of the Bankruptcy Act? (11 U.S.C. 110(e))

ARGUMENT

The Bankruptcy Act, Section 70(e)(1), expressly empowers the Trustee to avoid transfers or obligations

incurred, which obligation or transfer is voidable under state or Federal law by any creditor having a provable claim. *Crenshaw v. McKinley* (CCA 2d 1941) 116 F.2d 877, and *Pirie v. Chicago T & T Company,* 182 U.S. 438 (1901).

The point raised by the Appellant in this opening brief is that the collateral assignment between the "creditor" and the bankrupt is voidable under Section 70(e) of the Bankruptcy Act on the basis: (1) Federal Law, that the mortgage is an inchoate transfer, and that under Federal law, Section 6323 of the Internal Revenue Code of 1954, the United States' lien is prior to the lien of the "creditor," and the "creditor's" instruments were inchoate and unperfected under Section 6323 of the United States Internal Revenue Code, and therefore, the "creditor" is not entitled to the protection given by these statutes to a mortgagor, purchaser, or assignee; (2) State Law, that the transaction between the "creditor" and the bankrupt did not comply with the laws of the State of Arizona for the recording of instruments, and therefore, is not a prior lien to the lien of the Trustee herein.

Federal Law

Where the Trustee invokes Section 70(e) of the Bankruptcy Act, he must then demonstrate that he is asserting the right of a creditor or creditors of the bankrupt, against whom the particular transfer or obligation was fraudulent and voidable. *Hartman v. Lauchli* (CCA 8th 1956) 238 F.2d 881, cert. den. 353 U.S. 965 (1957); in re *Dipierro,* 159 F. Supp. 497 (1958).

Although the Trustee under Section 70(e) asserts the rights of creditors, he does so in his capacity as

Trustee, and is therefore endowed with whatever status the Act confers upon him in that capacity. *Peacock v. Fairbairn,* 45 I. 628, 264 Pac. 231. *Timmer v. Talbot* (D.C. Mich. 1936) 19 F. Supp. 687, aff'd. (CCA 6th) 89 F.2d 1011.

The creditors whose rights the Trustee invokes must be one "having a claim provable under this act." The claim which the Trustee proceeds under is that claim of the United States of America as expressed in its recorded lien and its claim on file herein, of which no contest is made in these proceedings.

The question then presented is whether the transaction between the "creditor" and the bankrupt is such that the transaction can be avoided by the United States as a creditor. The United States filed a tax lien and recorded said lien prior to the recording of any instruments showing title to the bankrupt's property in the "creditor." Therefore, the Trustee, under Section 70(e)(1), can also avoid the lien of the "creditor." (See cases cited above.)

It is the contention of the Trustee that the lien of the "creditor" is inchoate and unperfected, and therefore, the Trustee steps into the shoes of the United States as a creditor and therefore has a prior lien to that of the "creditor." *Ball Construction v. Jacobs,* 78 S. Ct. 442 (1958), reversing 140 F. Supp. 60. "The instrument involved being inchoate and unperfected, the provisions of § 3672(a) . . . (of the Internal Revenue Code) do not apply."

Various tests have been set forth by the courts to determine if a lien is inchoate and these are set forth as follows. Under these tests the alleged lien of the "creditor" is inchoate under all of the tests set forth below.

(a) The identity of the lienors was not fixed (because the lien was secret for lack of recordation). *United States v. Knott*, 298 U.S. 544, 56 S. Ct. 902 (1936).

(b) Neither title nor possession was in the "creditor." *United States v. Gilbert Associates*, 345 U.S. 361 (1953); *United States v. Carroll Construction*, 346 U.S. 802 (1953), reversing 249 P.2d 234.

(c) The "identification" of the property subject to the lien was not specific and consistent, *United States v. Texas*, 314 U.S. 480 (1941), for the reason that parcels could be released and the lien was not recorded; if the "creditor's" claim is made on the collateral assignment for the reason it was not recorded. The court is referred to: *United States v. Scovil*, 348 U.S. 218 (1955), reversing 78 S.E.2d 277; *United States v. Colotta*, 350 U.S. 808 (1955), reversing 79 So.2d 474; *United States v. White Bear Brewing Co.*, 350 U.S. 1010 (1956), reversing 227 F.2d 359; *United States v. Vorreiter*, 355 U.S. 15 (1957), reversing 307 P.2d 475.

One of the chief objectives of a recording statute is to prevent the obtaining of credit for the completion of a transfer of interest in property that is actually covered by a secret lien or conveyance. *General Motors Acceptance Corporation v. Collier*, (CCA 6th) 106 F.2d 584, cert. den. 309 U.S. 682, 60 S. Ct. 723. *Bank of America National Trust and Savings Association v. Sampsell*, (CCA 9th 1940) 114 F.2d 211.

The words of the United States District Judge as to the question of mortgages were brief and set forth the point clearly. He said,

"The collateral assignment constitutes an unre-

corded mortgage of real property, and the recording of the deed from the Peabodys to Phoenix Title & Trust Company, as Trustee, was not notice of such collateral assignment to the creditors of the Peabodys. Accordingly, the collateral assignment is voidable under Section 70(c) of the Bankruptcy Act."

In 1961 the Supreme Court, in the famous case of *Lewis v. Manufacturers National Bank of Detroit*, 364 U.S. 603, the court made the following comment:

> "We think that one consistent theory underlies the several versions of § 70c which we have set forth, *viz.*, that the rights of creditors — whether they are existing or hypothetical — to which the trustee succeeds are to be ascertained as of 'the date of bankruptcy,' not at an anterior point of time. That is to say, the trustee acquires the status of a creditor as of the time when the petition in bankruptcy is filed. We read the statutory words 'the rights .. . of a creditor (existing or hypothetical) then holding a lien' to refer to that date. This construction seems to us to fit the scheme of the Act. *Section 70e enables the trustee to set aside fraudulent transfers which creditors having provable claims could void.* The construction of § 70c which petitioner urges would give the trustee power to set aside transactions which no creditor could void and which injured no creditor. That construction would enrich unsecured creditors at the expense of secured creditors, creating a windfall merely by reason of the happenstance of bankruptcy." (Emphasis supplied)

With the lien of the "creditor" being inchoate, the Trustee under Section 70(e) should prevail, and should have a lien prior to any lien of the "creditor."

State Law

Arizona Revised Statutes §§ 33-412A and 33-702

are set forth in full as they are controlling on the subject of recording instruments which are either mortgages or trusts.

Arizona Revised Statutes § 33-412A:

"Invalidity of unrecorded instruments as to bona fide purchaser or creditor.

A. All bargains, sales and other conveyances whatever of lands, tenaments and hereditaments, whether made for passing an estate of freehold or inheritance or an estate for a term of years and deeds of settlement upon marriage whether of land, money or other personal property, and deeds of trust and mortgages or whatever kind, shall be void as to creditors and subsequent purchasers for valuable consideration without notice, unless they are acknowledged and recorded in the office of the county recorder as required by law, or where record is not required, deposited and filed with the recorder."

Arizona Revised Statutes § 33-702:

"Mortgage defined; pledge distinguished; admissibility of proof that transfer is a mortgage.

"Every transfer of an interest in property, other than in trust, made only as a security for the performance of another act, is a mortgage, except a transfer of personal property accompanied by an actual change of possession, which is deemed a pledge. The fact that a transfer was made subject to defeasance on a condition, may, for the purpose of showing that the transfer is a mortgage, be proved except against a subsequent purchaser or encumbrancer for value and without notice, notwithstanding that the fact does not appear by the terms of the instrument."

These sections specifically state that every transfer, other than a trust, is a mortgage. This section states that the deed to the Trust Company is not a

mortgage and cannot be foreclosed as one. Therefore, the rights, if any, claimed by the "creditor" must arise under the *collateral assignment*. This term is used advisedly as discovery of the trust instrument would give no notice of any security device, because by the terms of that instrument, the Peabodys are the beneficiaries and not the "creditor." Quoting from the words of the District Judge relative to the issue of whether trust creates an interest in personal property, the judge said,

> "Even if it were concluded that the trust is active and that the interest of the Peabodys is personal property, it would appear that the collateral assignment constitutes an unfiled mortgage of personal property (other than crops growing or to be grown or animate personal property), void as to subsequent creditors of the Peabodys. Arizona Revised Statutes, §§ 1-215, subdivision 22; 33-751; and 33-753, subdivision 5."

The fact that the transaction, as between the parties might be binding contractually and a valid lien exists *inter se* does not defeat other creditors' liens and those of the Trustee.

> "It is not enough that the purported assignment might have been valid as between the parties. The statute prescribes the form, manner, execution, and delivery of assignments and its contents." *Lawrence v. Delta Metals, Inc.*, (CA 5th 1960) 280 F.2d 86.

A typical reported case, though old, sheds light on the failure to properly record, the failure in this case being failure to record the collateral assignment. *Joseph vs. Winakur*, (CCA 4th Cir. 1929) 30 F.2d 510. This case holds failure to record is a fatal error as to a lien.

CONCLUSION

It is therefore respectfully submitted that under both Federal and state law the Trustee under Section 70(e), in addition to his rights under Section 70(c) of the Bankruptcy Act, is prior in time and right to the "creditor" in this case, and the order of the Referee as to his ruling, under Section 70(e), be sustained and the order of the District Judge be sustained on this additional ground.

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APPENDIX

United States Bankruptcy Act:

Section 70(c).

The Trustee may have the benefit of all defenses available to the bankrupt as against third persons, including statutes of limitation, statutes of frauds, usury, and other personal defenses; and a waiver of any such defense by the bankrupt after bankruptcy shall not bind the trustee. The trustee, as to all property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt could have obtained a lien by legal or equitable proceedings at the date of bankruptcy, shall be deemed vested as of such date with all the rights, remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such a creditor actually exists.

Section 70(e).

(1) A transfer made or suffered or obligation incurred by a debtor adjudged a bankrupt under this Act which, under any Federal or State law applicable thereto, is fraudulent as against or voidable for any other reason by any creditor of the debtor, having a claim provable under this Act, shall be null and void as against the trustee of such debtor.

(2) All property of the debtor affected by any such transfer shall be and remain a part of his assets and estate, discharged and released from such transfer and shall pass to, and every such transfer or obligation shall be avoided by, the trustee for the benefit of the estate: *Provided, however,* That the court may on due notice order such transfer or obligation to be preserved for the benefit of the estate and in such event the trustee shall succeed to and may enforce the rights of such transferee or obligee. The trustee shall

reclaim and recover such property or collect its value from and avoid such transfer or obligation against whoever may hold or have received it, except a person as to whom the transfer or obligation specified in paragraph (1) of this subdivision e is valid under applicable Federal or State laws.

Internal Revenue Code of 1954:

Section 6323. Validity Against Mortgagees, Pledgees, Purchasers, and Judgment Creditors.

(a) Invalidity of Lien Without Notice. Except as otherwise provided in subsection (c), the lien imposed by section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the Secretary or his delegate.

(1) Under State or Territorial Laws. In the office designated by the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law designated an office within the State or Territory for the filing of such notice; or

(2) With Clerk of District Court. In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State or Territory has not by law designated an office within the State or Territory for the filing of such notice; or

(3) With Clerk of District Court for District of Columbia. In the office of the clerk of the United States District Court for the District of Columbia, if the property subject to the lien is situated in the District of Columbia.

(b) Form of Notice. If the notice filed pursuant to subsection (a) (1) is in such form as would

be valid if filed with the clerk of the United States district court pursuant to subsection (a) (2), such notice shall be valid notwithstanding any law of the State or Territory regarding the form or content of a notice of lien.

(c) Exception in Case of Securities.

(1) Exception. Even though notice of a lien provided in section 6321 has been filed in the manner prescribed in subsection (a) of this section, the lien shall not be valid with respect to a security, as defined in paragraph (2) of this subsection, as against any mortgagee, pledgee, or purchaser of such security, for an adequate and full consideration in money or money's worth, if at the time of such mortgage, pledge, or purchase such mortgagee, pledgee, or purchaser is without notice or knowledge of the existence of such lien.

(2) Definition of Security. As used in this subsection, the term "security" means any bond, debenture, note, or certificate or other evidence of indebtedness, issued by any corporation (including one issued by a government or political subdivision thereof), with interest coupons or in registered form, share of stock, voting trust certificate, or any certificate of interest or participation in, certificate of deposit or receipt for, temporary or interim certificate for, or warrant or right to subscribe to or purchase, any of the foregoing; negotiable instrument; or money.

(d) Disclosure of Amount of Outstanding Lien. If a notice of lien has been filed under subsection (a), the Secretary or his delegate is authorized to provide by rules or regulations the extent to which, and the conditions under which, information as to the amount of the outstanding obligation secured by the lien may be disclosed.

Arizona Revised Statutes:

Section 1-215, subdivision 22. Definitions.

22. "Personal property" includes money, goods, chattels, dogs, things in action and evidences of debt.

Section 33-751. Types of personal property which may be mortgaged.

Mortgages may be made upon:

1. All growing crops.

2. All kinds of personal property except on a stock of goods, wares or merchandise daily exposed to sale as set forth in the provisions of § 33-752. As Amended Laws 1956, Ch. 159, § 1.

Section 33-753. Requirements of validity of mortgage.

A mortgage of personal property or crops is void as against creditors of the mortgagor and subsequent purchasers and encumbrances of the property in good faith and for value, unless:

1. The mortgage is acknowledged in like manner as instruments of conveyance of real property.

2. The mortgage, if of animate personal property other than crops growing or to be grown, is filed in the office of the recorder of the county where the mortgagor resides at the time the mortgage is executed, or if the mortgagor is a nonresident of this State, in the office of the recorder of the county where the property mortgaged is located at the time the mortgage is executed.

3. The mortgage, if of crops growing or to be grown, is filed in the office of the recorder of the county where the land is lo-

cated upon which such crops are growing or to be grown.

4. The mortgage, if of personal property other than crops growing or to be grown or animate personal property, is filed in the office of the recorder of each of the counties where the property mortgaged is located and where the mortgagor resides at the time the mortgage is executed, provided that in case the mortgagor is a nonresident of this state, no filing where the mortgagor resides is required, and, if the property mortgaged is thereafter removed to another county of this state, either the mortgage is filed in that county or there is or has been filed a statement of recordation as prescribed in § 33-754.

5. The mortgage is clearly designated on its face, apart from and preceding the terms of the mortgage, to be a mortgage of crops and chattels, or either.

6. Within six years from the last filing or refiling, the mortgage is filed in its entirety, or in lieu thereof there be filed a certification executed by the mortgagor or mortgagee, or the successor in interest of either, and filed in the office of the recorder of each county in which the mortgage has been filed. The certificate shall be in substantially the following form:

Certificate of Refiling

By this certificate of refiling that certain mortgage made by ....., mortgagor, of ....., to ....., mortgagee, of ....., and dated the ..... day of ....., in the year ....., and filed in the office of

the recorder of the county of ....., on the ..... day of ....., in the year ....., and abstracted in book ..... of ....., at page ..... (set forth if available the date and place of each filing), be and the same hereby is refiled.

(Signed) A.B. or C.D.

The certificate shall be acknowledged in like manner as conveyances of real property. No certificate shall be deemed defective because it does not refer to all of the filing data of the original mortgage. The provisions of this subparagraph shall not apply to any mortgage heretofore or hereafter made pursuant to an order, judgment, or decree of court of record, or heretofore or hereafter made to secure the payment of bonds or other evidences of indebtedness authorized or permitted to be issued under jurisdiction of the Arizona corporation commission. The term "refiling" as used in this section shall include the refiling of a certificate of refiling. As amended Laws 1956, Ch. 159, § 3.

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

NO. 18819

MYLES STEWART, Trustee of the Estate of ARTHUR PEABODY and OLIVE PEABODY,
Appellants,

vs.

PHOENIX TITLE & TRUST COMPANY,
Appellee.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

.....

CLAGUE A. VAN SLYKE
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182 North Court
Tucson, Arizona

IN THE

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JURISDICTIONAL STATEMENT

Appellees agree that this is an appeal from an Order entered on March 29, 1963, affirming in part the Order of the Referee in Bankruptcy entered on May 31, 1962.

Jurisdiction of the Referee in Bankruptcy is under the provisions of Title 11 Bankruptcy Sec. 11(a)(7) United States Code, that of the District Court und and by virtue of the provisions of Title 11 Bankruptcy Section 11(a)(10) United States Code and that of this Court under Title 11 Bankruptcy Section 47 United States Code.

STATEMENT OF THE CASE

Appellee under his brief as appellant in the case of Phoenix Title & Trust Company, Appellant, v. Arthur Peabody and Olive Peabody, Appellees, limited their presentation to the specification of errors set forth on page 9 and the questions presented on page 10 of said brief. Myles Stewart, Trustee, Appellant, in the specification of errors set forth on page 10 of the Appellant's brief attempts to reverse the District Court's ruling under Sec. 70(e) of the Bankruptcy Act. Since the arguments go beyond this specification of error and attempts to answer in anticipation Phoenix Title and Trust Company Appellant's brief, in this brief it will be necessary in addition to the proposition that Sec. 70(e) of the Bankruptcy Act is not applicable in the present situation to discuss matters raised in Appellant Phoenix Title and Trust Company's brief when absolutely necessary to answer Appellant Stewart's brief.

FACTS IN THIS CASE

Appellee incorporates by reference the Statement of the Case of Phoenix Title and Trust Company Appellant's brief covered on pages 2 through 8 thereof. It further accepts Appellant Stewart's Statement of Facts set forth on page 3 through 9 thereof where they are statement of facts, but denies specifically Appellant's interpretation of the intentions of the parties or their conclusions growing out of the instruments and the actions involved.

Appellee, Phoenix Title and Trust Company, specifically denies the allegation on page 4 to the effect Arthur Peabody and Olive C. Peabody were in possession and control of the property at the time of bankruptcy with all powers of management, charged with full responsibility for the handling of the property in carrying out the stated

purposes of the trust, alleging that there is no evidence to support that statement, specifically alleging that all evidence was to the effect that at all times since June 1, 1957, Phoenix Title and Trust Company was in sole and exclusive possession of all the property described in the Trust Deed. (lines 1 through 4, page 72, TR)

With reference to the allegation on page 4 of Apellant Stewart's brief that neither the Trust Deed nor the Trust Agreement refer specifically to other instruments executed by the Peabodys as security, this is denied and Appellee specifically alleges that both documents provide for such contingencies all as set forth in detail in Phoenix Title and Trust Company Appellant's brief.

The Appellee specifically denies the first paragraph on page 5 and believes that the Appellants have stated their conclusions and wishes but that the facts and the simultaneous execution of all instruments force one to the opposite conclusions.

ARGUMENT

Cross-appellant, the Trustee in Bankruptcy, appeals from the Order on Review of the District Court of March 29, 1963, (TR 171) and in his brief (p. 10) specifies that the District Court erred in not sustaining paragraphs 11 and 13 of the Referee's Conclusions of Law (TR 134). By these conclusions the Referee determined (1) that the Trustee in Bankruptcy under Sec. 70(e) of the Bankruptcy Act could be subrogated to the position of the United States as a creditor under its tax lien (notice of which was recorded subsequent to recordation of the Trust Deed, (Exhibit 2), and (2) that the lien of Phoenix Title and Trust Company is inchoate and that applying the doctrine of choateness of lien referrable to the enforcement of Federal tax liens the Trustee, so subrogated, could set aside the asserted inchoate lien

of Phoenix Title and Trust Company.

The argument of Cross-appellant, the Trustee in Bankruptcy, does not substantiate the above-described action of the Referee with respect to Conclusions of Law 11 and 13; rather, Cross-appellant cites cases illustrating the doctrine of choateness of lien but confuses this doctrine with assertions that Cross-appellee's mortgage lien is *"an inchoate transfer"* and that Cross-appellee's *"instruments were inchoate" and unperfected under Section 6323 of U. S. Internal Revenue Code."* Accordingly, Cross-appellant's argument has nothing to do with the action of the Referee as reflected in Conclusions 11 and 13, so that for purposes of clarity Cross-appellee, Phoenix Title and Trust Company, will first answer the general assertion that the Referee's action as reflected in Conclusions 11 and 13 was correct, and will next answer Cross-appellant's argument which appears to assert defects in the recording of Cross-appellee's lien, which, if true, would vitiate Phoenix Title and Trust Company's lien under Section 70(c) of the Bankruptcy Act rather than under Section 70(e) of that Act.

I
TAX LIEN ASPECTS

The Referee erred in his Conclusions of Law 11 and 13 in subrogating the Trustee (under Sec. 70(e) of the Bankruptcy Act) to the position of the U.S. as a tax lien holder and asserting the doctrine of choateness of lien to vitiate Cross-appellee's lien for the following reasons:

1. The doctrine of choateness of lien referrable to insolvency statutes and Federal tax liens under the Federal priority statutes is not applicable in situations under the Bankruptcy Act. *U.S.* v. *Cargill,* Cir.

1, 218 F.2d, 556, 558; *In Re Taylorcraft Aviation Corporation,* Cir. 6, 168 F.2d, 808, 97 L.Ed. 47; *U.S.* v. *Sampsell,* Cir. 9, 153 F.2d, 731, 734.

2. The Trustee in Bankruptcy cannot be subrogated (under Sec. 70(e) of the Bankruptcy Act) to the position of a government as a creditor where the laws creating such creditor relationship are specifically intended to benefit only that government and not creditors generally. *In the Matter of F. A. Whitney Carriage Company,* 173 F. Supp. 709; *Silverman* v. *Wedge,* 158 NE 2d, 668.

3. The creditor contemplated by the Subrogation Statute, Sec. 70(e) of the Bankruptcy Act, is a creditor in the conventional sense. By analogy see: *In the Matter of Ben Green, Bankrupt,* D.C. Ala. 124 F. Supp. 481; *U.S.* v. *Gilbert Associates,* 345 U.S. 361; *U.S.* v. *Security Trust and Savings Bank,* 340 U.S. 47.

4. "Applicable Federal Law" as used in Sec. 70(e) of the Bankruptcy Act refers to Federal law involving property rights and not police measures, e.g. *Benner* v. *Scandinavian American Bank,* 131 Pac. 1149; *Arnold* v. *Eastin's Trustee,* 76 SW 855.

A. *The Doctrine of Choateness of Lien*

As an adjunct of the Federal priority statutes (Sec. 3466 Revised Statutes, 31 USCA §191) the doctrine of choateness of lien was established, beginning in 1933 with *New York* v. *Maclay,* 288 U.S. 290 and culminating with *U.S.* v. *Security Trust and Savings Bank,* 340 U.S. 47, in 1950 (with respect to competing liens). In its inception the doctrine was applied to insolvency situations where bankruptcy under the Bankruptcy Act was not involved. Subsequently, the doctrine

has also been regularly applied in cases involving Federal tax liens where bankruptcy under the Bankruptcy Act is not involved.

Past attempts to apply the doctrine of choateness of lien to situations under the Bankruptcy Act have been consistently rejected where Sec. 64—the priority section of the Bankruptcy Act—was involved. Thus, in *U.S.* v. *Cargill,* 218 F.2d, 556, 558, the Court of Appeals for the First Circuit stated:

> "We shall first deal with the Government's contention that the district court was in error when it failed to apply the federal priority statute which gives the Government priority for its claims in the event of a debtor's insolvency and the commission of an act of bankruptcy. *The weight of authority indicates that this statute is not applicable in proceedings in bankruptcy.* 4 Collier on Bankruptcy, 264 and n. 51 (14th ed. 1954); see *Adams* v. *O'Malley,* 8 Cir., 1950, 182 F.2d 925; *United States* v. *Sampsell,* 9 Cir., 1946, 153 F.2d 731; *In re Knox-Powell-Stockton Co.,* 9 Cir., 1939, 100 F.2d 979. *It cannot be assumed that Congress was so illogical and inconsistent as to enact §64 of the Bankruptcy Act, 11 U.S.C.A. §104, entitling the Government only to a fourth priority insofar as its tax claims are concerned and a fifth priority as to certain other debts owed to the United States, if it did not intend that §64 supercede,* insofar as bankruptcy proceedings are concerned, the first priority given to federal claims under §3466." (emphasis supplied) *U.S.* v. *Cargill,* 218 F.2d 556 at 558.

The Sixth Circuit in *In Re Taylorcraft Aviation Corporation,* 168 F.2d 808, 810, held that the doctrine of choateness of lien did apply because bankruptcy was not involved:

> "The case therefore involves the priority of one lien over another, and §3466, R.S., Title 31 U.S.C., §191, 31 U.S.C.A. §191 and §104, Title 11, U.S.C., 11

U.S.C.A. §104, are not involved. We think the problem is not solved by the citation of the decision of the *United States Supreme Court in New York* v. *Maclay,* 288 U.S. 290, 53 S.Ct. 323, 77 L.Ed. 754; *United States* v. *Texas,* 314 U.S. 480, 62 S.Ct. 350, 86 L.Ed. 356; *Illinois* v. *United States,* 328 U.S. 8, 66 S.Ct. 841, 90 L.Ed. 1049; and *United States* v. *Waddill, Holland & Flinn, Inc., supra. These cases did not involve bankruptcy proceedings, and therefore the priority provision of §3466 was applicable to these decisions.*" (emphasis supplied.)

The leading case rejecting the doctrine of choateness of lien is *U.S.* v. *Sampsell,* Cir. 9, 153 F.2d 731. At page 735 the Court stated:

"Section 64 does not give taxes of the United States or of a state priority of payment over *valid existing liens under §67, since such liens are not affected by the Bankruptcy Act.* Section 67 applies against the United States just as it does against any creditor. A lien does not have to be specific or perfected lien to come within the protection of §67. The cases which have held that only perfected liens are given priority are within the §3466 of the Revised Statutes, 31 U.S.C.A. §191, but that section does not apply to bankruptcy proceedings, hence its all-inclusive effects do not cover the situation in this case." (emphasis supplied)

The only case where bankruptcy was involved and where the doctrine of choateness of lien was applied is *U.S.* v. *Reese,* Cir 7, 131 F.2d 466. The Ninth Circuit specifically overruled that case stating:

"The cases cited by the government, with the exception of *United States* v. *Reese,* 7 Cir., 1942, 131 F.2d 466, do not involve bankruptcy proceedings and hence are not applicable in the instant controversy. It has been established that §3466 of the Revised Statutes, 31 U.S.C.A. §191, does not apply in the bankruptcy proceedings so that the cases cited by the government, in holding that inchoate liens will

not defeat the priority of the government's liens established by that section, do not control the instant case." (pg. 734)

"The case of *United States* v. *Reese,* 7 Cir., 1942, 131 F.2d 466, is not controlling here, since there was a failure in that case to consider the applicable provisions of the Bankruptcy Act, the governing statute, and also because it relies upon authorities which are inapplicable under the Bankruptcy Act." *U.S.* v. *Sampsell,* 153 F.2d 731, 735.

Section 67 protects valid existing liens even though they be not specific or perfected if they otherwise meet the requirements of §67. By implication this case also would reject the possibilities of subrogating the Trustee to the position of the United States as a tax creditor under §70(e) because to do so would then deny the protection of §67 which the Court of Appeals for the Ninth Circuit declares protects liens otherwise meeting its requirements even though they be not specific or perfected.

A moment's reflection on the history of the Bankruptcy Act will show that the Sampsell case governs §70(e) of that Act as well as §64 wherever Federal tax liens are involved:

Sec. 63 of the Act of 1800: "That nothing contained in this act shall be taken, or construed to invalidate or impair any lien existing at the date of this act . . ." *Sec. 2 of the Act of 1841:* ". . . and provided also, that nothing in this act contained shall be construed to amend, destroy, or impair . . . any liens, mortgages, or other securities or property, real or personal, which may be valid by the laws of the States respectively."

With respect to the above quoted sections of the earlier law, *Colliers,* 14th Edition, Vol. 4, page 37, states:

"*Section 67d of the Act of 1898 was intended to be*

a savings clause, serving the same function as §63 of the Act of 1800 and the proviso of §2 of the Act of 1841." (empahsis supplied)

The dissenting opinion of Justice Frankfurter in the recent case of *Simonson* v. *Granquist* (while rendered in connection with facts completely unrelated here) summarizes the status of the lien in Bankruptcy as follows:

> "Congress has thus treated liens as outside the policy of equal treatment of creditors in bankruptcy. 3 Collier supra, ¶57.07. A lienor does not hold simply a first priority; he has "a right to enforcement independent of bankruptcy." id., ¶64.02, at 2061. The Bankruptcy Act deals with the distribution of unencumbered assets among unsecured creditors. id., ¶60.01. Lienholders need no Bankruptcy Act. Liens are independent of and essentially unaffected by bankruptcy proceedings." *Simonson* v. *Granquist*, 369 U.S. 38; 62-1 USTC #9298 at 83,770

From the foregoing the conclusion, inescapably, must be just as §67(d) in the Sampsell case protected a valid existing lien from the priority operation of §64 of the Bankruptcy Act as respects taxes just as much does §67 protect valid and existing liens from the tax lien choateness of lien doctrine asserted through subrogation under 70(e). If the court in Sampsell refused to allow the use of that doctrine through §64 to destroy otherwise valid and existing liens, what compelling reason suggests that it would allow the same thing through §70(e)?

Parenthetically, it should be noted that if the Referee is correct in applying the doctrine of choateness of lien through Sec. 70(e) of the Bankruptcy Act, his Conclusion of Law No. 14 (TR 134) upholding the mechanic's lien of Midway Lumber Company which is clearly inchoate (not having been reduced to judgment—*U.S.* v. *White Bear Brewing Company*, 350 U.S. 1010) is incorrect. Carried to its logical conclusion, if

the Trustee were permitted to assert the doctrine of choateness of lien through §70(e) of the Bankruptcy Act, he would would then be able to avoid any statutory mechanics' liens valid under Sec. 67(d) by using Section 70(e) which doesn't merely relegate the lien under attack to an inferior position by its terms but has the unique effect of opening up the entire field, setting aside entirely the liens of all such creditors, if it can be utilized. Other statutory liens such as mortgages securing future advances on crops, etc., as authorized by 33-773 Arizona Revised Statutes would be vitiated, together with open-end real estate mortgages as now protected under Arizona law; *Griffith* v. *State Mutual Building and Loan Association,* 46 Ariz. 359. Thus, it is conceivable that a $1 Federal tax lien could destroy the entire security of a $5,000,000 shopping center if Section 70(e) could be applied as is urged in this case by the Trustee and ordered by the Referee.

B. *The Trustee may not be subrogated under §70(e) to the position of a government as a creditor.*

An attempt similar to the ruling made in this case, using §70(e) of the Bankruptcy Act, occurred in Massachusetts when the Referee subrogated the Bankruptcy Trustee to the position of the State of Massachusetts as a creditor for corporate taxes to void a prior chattel mortgage.

The United States District Court for Massachusetts held:

> "Even if it could be held that the Massachusetts statutes covered a mortgage transaction I still do not feel that the Trustee could succeed to the rights of the Commonwealth of Massachusetts where that right was granted only to the Commonwealth. To give it the effect that the Trustee seeks would do great harm to our economic system. It is not enough

to say that the language of both Acts is clear and unambigious and that the Court should not attempt to legislate, but should merely apply the laws as found. This is true of course, but the Court should take a realistic view of the purposes intended to be accomplished by both the Massachusetts Laws and the Bankruptcy Act and should apply common sense in reaching its decision."

In the Matter of F. A. Whitney Carriage Company 173 F. Supp. 709 at page 711 (Nov. 30, 1953)

Five-and-a-half years later the same proposition with the same Massachusetts tax law was raised in an attempt to set aside a truck sale; the Massachusetts Supreme Court held:

"The decision then indicated that, even if §76 was applicable at all, 11 U.S.C. (1952) §110, sub. e(1) (11 U.S.C.A. §110, sub. e(1) did not in fact apply to §76, for the reason that the latter was intended to give the Commonwealth a peculiar right which a trustee in bankruptcy was not empowered to assert for the benefit of general creditors. In Matter of F. A. Whitney Carriage Co., D.C. 173 F. Supp. 709." (§76 refers to the Mass. corporate tax law)

Silverman v. *Wedge,* 158 N.E.2d, 668 at 669 (May 18, 1959)

C. *The creditor contemplated by §70(e) is the conventional creditor.*

The conventional creditor under §70(e): The position of the creditor to which the Trustee in Bankruptcy may be subrogated is obviously by Federal law intended to be a *creditor in the conventional* sense. Some indication of this proposition exists *In the Matter of Ben Green, Bankrupt,* D.C. Ala. 124 Fed. Sup. 481; in construing a "judgment creditor" under the protection of the Internal Revenue Code where a Trustee in Bankruptcy attempted to distribute a bankrupt's estate to the State of Alabama

by avoiding the government's lien for Federal taxes, the court held that the State Department of Industrial Relations of Alabama was not a "judgment creditor" as contemplated within the protection of the Internal Revenue Code. The court at page 481 stated that:

> "Judicial gloss placed upon the words 'judgment creditor' as employed by Congress in Sec. 3672 (predecessor to Sec. 6323 of the present Act) conclusively establishes that such words were used "in the usual, conventional sense of a judgment of a court of record'; United States v. Gilbert Associates, at 345 US 361, United States v. Security Trust and Savings Bank at 340 US 47."

With respect to these last two cited cases the court in the Green cases said:

> "Concededly, neither of these cases was dealing with bankruptcy. If the trustee in bankruptcy in the instant proceeding (*wherein there is no conventional judgment creditor to whose rights the trustee would succeed by operation of Section 70, sub. e* of the Act) is endowed with the status of a judgment creditor, it must be because of the provisions of Section 70, sub c of the Bankruptcy Act . . .," (emphasis supplied) "No one may doubt the authority of Congress to constitute a trustee in bankruptcy a judgment creditor with reference to federal tax laws. Clear and appropriate language to that end might have been included in Section 70, sub c of the Act, but obviously was not. Or, Congress might have added trustees in bankruptcy to the categories of persons described in 26 U.S.C.A. §3672(a), as against whom the lien created by 26 U.S.C.A. §3670 is invalid until notice thereof has been filed by the collector as required by law, but it did not. *Nor did it include the trustee in bankruptcy in the corresponding section 6323* of the Internal Revenue Code of 1954, . . ." (emphasis supplied)
>
> *Matter of Green*, 124 F. Supp. 481, 482

From the foregoing *italicized* portion of the

Green opinion, it will be seen that the court before ruling on the contention of the Trustee that it was a "judgment creditor" protected under the tax laws, first considered the possibility of subrogating the Trustee under Sec. 70(e) of the Bankruptcy Act but rejected the State Department of Industrial Relations as subrogee because it was not a conventional creditor under the meaning of Section 70(e).

D. *Applicable Federal Law*

Section 70(e) of the Bankruptcy Act makes void against the Trustee "a transfer . . ., which under any Federal or State law applicable thereto, is . . . voidable . . . by any creditor of the debtor." There are no cases, apparently, applying "applicable federal law." Logic compels that the statute means Federal law equivalent to state law (as in the District of Columbia and U. S. Territories) and that such Federal law defines property rights in the same manner as "applicable state law" applies to creditors; such creditors in each case have property rights—assignable, transferable property rights —which they seek to assert as superior to the property rights of others. The Federal government's rights as a mortgagee or other conventional creditor, or the rights of a conventional creditor within the District of Columbia or under maritime laws and the like (see *Benner* v. *Scandinavian American Bank,* 131 Pac. 1149, and *Arnold* v. *Eastin's Trustee,* 76 SW 855, holding bill of sale and mortgage respectively not valid since not recorded in accordance with Federal statute) clearly should fall within the concept:

"federal . . . law applicable thereto."

But the right of the Federal government to collect taxes is not a property right; it is a *police* power and the manner in which it may be asserted, as through the doc-

trine of inchoateness of lien, can scarcely have been contemplated by Congress as an object for subrogation under Sec. 70(e).

II
APPLICABLE LAW

Is there, as asserted by Cross-appellant, a principle of law that an "inchoate transfer" under Federal Law, Sec. 6323 of the Internal Revenue Code of 1954 is voidable under Section 70(e) of the Bankruptcy Act, or is there a principle of law that provides that where instruments are "inchoate and unperfected under Section 6323 of the U. S. Internal Revenue Code," the creditor owning such instruments is not entitled to protection given by Section 6323, Internal Revenue Code to a "mortgagor, purchaser or assignee"; and finally, does the security device of Phoenix Title and Trust Company (represented by the Trust Deed, Exhibit 2, Trust Agreement, Exhibit 3, Promissory Note, Exhibit 4, and Collateral Assignment, Exhibit 5) comply with the laws of the State of Arizona for the recording of instruments so that it is prior to any claim which the Trustee in Bankruptcy may assert under Sec. 70(c) or Sec. 70(e) of the Bankruptcy Act.

A. *Federal Law*

The first two of the above questions asserted by the Trustee in Bankruptcy in his cross-appeal are set forth on page 11 under the category "Federal Law" and it appears to be the position of the Bankruptcy Trustee that the mortgage of Phoenix Title and Trust Company is not entitled to protection under the Bankruptcy Law as a mortgage device unless it constitutes a valid mortgage under Sec. 6323 of the Internal Revenue Code of 1954. In the first place, the Bankruptcy Act and the Internal

Revenue Code are mutually exclusive. If it is the position of Cross-appellant that Phoenix Title and Trust Company, to establish the validity of its lien, must satisfy the Internal Revenue Code definition of a mortgage under Sec. 6323 of the Internal Revenue Code of 1954, by the same token it would logically follow that the Trustee to assert his superior position should be able to qualify as a "judgment creditor" under the protection of the same statute, Sec. 6323, Internal Revenue Code, but attempts in similar cases have failed completely in that respect. See *In the Matter of Ben Green, Bankrupt,* supra.

The Green case sets forth the Federal Court's position that a Trustee in Bankruptcy simply does not come under the protection of Sec. 6323 of the Internal Revenue Code. The reason is, of course, that the Bankruptcy Act and the Federal tax laws are mutually exclusive. Thus, *In the Matter of Fidelity Tube Corp. et al,* 3 S. Cir. 167, Fed. Supp. 402 at page 403 in defining a judgment creditor within the purview of Sec. 3672 (now Sec. 6323) of the Internal Revenue Code the Court quoted with approval the following:

> "In this instance we think that Congress used the words 'judgment creditor' in §3672 in the usual, conventional sense of a judgment of a court of record, since all states have such courts."

Again, the courts have refused to clothe the Trustee in Bankruptcy with other protective benefits of the Internal Revenue Act, such as those of an employee under Sec. 1303 of the Internal Revenue Code as respects the back-pay of relief provisions of that Act. Thus, in *Williamson* v. *United States,* DC Kentucky 1961, 200 F. Supp. 689 at 691, the Court stated:

> "Had the Congress seen fit to include trustees as employees within the meaning of the statute it could

have said so. An employee and a trustee in bankruptcy are two entirely different things."

For the reasons above stated, and as stated in Part I of this brief, the contention that Phoenix Title and Trust Company as a mortgagee does not satisfy the definition of a mortgagee under Sec. 6323 of the Internal Revenue Code of 1954 is completely irrelevant. This is not a case of priority of a Federal tax lien over a mortgage lien; this is a question of a Trustee's rights under the Bankruptcy Act against a mortgage lien, and historically the Federal Courts have refused to clothe the Trustee in Bankruptcy with any more powers than given him under the Bankruptcy Act. Heretofore, no Court has recognized the contention that the Trustee in Bankruptcy may be impressed with superior powers arising under other Federal statute than those under the Bankruptcy Act, whether it be the Internal Revenue Code, the Federal Insolvency Statutes or any other section of the Federal Code. Logically, "federal law" to which Sec. 70(e) of the Bankruptcy Act refers in determining the rights of a creditor to whom the Trustee may be subrogated is federal law in the conventional sense. While Sec. 70(e) of the Bankruptcy Act makes void against the Trustee "a transfer . . ., which under any federal or state law applicable thereto, is . . . voidable . . . by any creditor of the debtor", there are, however, no cases applying "applicable federal law." Logic compels that the statute means federal law equivalent to state law (as in the District of Columbia and United States Territories) and that such federal law defines property rights in the same manner as "applicable state law" applies to creditors.

B. *State Law*

On page 14, Cross-appellant sets forth applicable portions of Arizona Revised Statutes in support of his

position that the Trustee in Bankruptcy may be subrogated to the position of a creditor under State law and under State recording acts avoid the lien of Phoenix Title and Trust Company. With respect to this latter contention, it is basic that if a hypothetical creditor exists as of the date of bankruptcy who could set aside the lien of Phoenix Title and Trust Company, then that lien may be avoided not under Sec. 70(e) but under Sec. 70(c) of the Bankruptcy Act. On the other hand, under Sec. 70(e) of the Bankruptcy Act, if an actual creditor existed as of anytime (as distinct from the date of bankruptcy) the the Trustee may be subrogated to the rights of that creditor as of the time that creditor's lien affixed.

Phoenix Title and Trust Company's position as heretofore set out is that the Federal government with its tax lien is not a creditor within the purview of Sec. 70(e) of the Bankruptcy Act, unless the Federal government is simply regarded as another creditor in the same category as any general creditor, subject to the established doctrine that first in time of recording is first in right; and it is not disputed that the Federal government (TR 133) filed its notice of tax liens (August 19, 1957) subsequent to the recording of the Trust Deed, Exhibit 2, (July 31, 1956) of Phoenix Title and Trust Company (TR 124). Therefore, if the record title of Phoenix Title and Trust Company is good, the Trust Deed having been recorded prior in time to that of any other instrument except Midway Lumber Company's Mechanics Lien (Exhibit 1), then it follows that Phoenix Title and Trust Company's lien is good against all other creditors, including the United States Government, irrespective of whether or not the Trustee is subrogated under Sec. 70(c) or 70(e).

Heretofore, Phoenix Title and Trust Company's brief (filed February 18, 1964) as Appellant under Part B, page 12 and following set forth the reasons and the authorities by which Phoenix Title and Trust Company claims the validity of its lien as of the date of recordation of Exhibit 2, the Trust Deed. The critical instruments involved in this appeal, the Trust Deed, Exhibit 2, Trust Agreement, Exhibit 3, Promissory Note, Exhibit 4, and Collateral Assignment of Beneficial Interest, Exhibit 5, were all executed and delivered concurrently on July 26, 1956. These instruments collectively constituted the security for Phoenix Title and Trust Company's advance of $50,000.00 to Arthur Peabody, the bankrupt. The Trust Deed was recorded on July 31, 1956. Cross-appellant has attempted, without legal authority, to divide these instruments into two categories—the Trust Deed and Trust Agreement being one category, the Promissory Note and Collateral Assignment being the other category, disregarding the fact that all four instruments were executed and delivered concurrently on the same date, to-wit: July 26, 1956. As previously stated, the general rule is that:

> "Where several instruments, executed contemporaneously or at different times, pertain to the same transaction, they will be read together although they do not expressly refer to each other."
>
> Vol. 17A, C.J.S. Sec. 298, Separate writings, page 128, Restatement of Contracts, 237C. *Clark* v. *Levy,* 25 Ariz. 541; 220 Pac. 232.

Substantially the same security device as used in this case was used in *Barringer* v. *Lilley,* 9 Cir. 96 Fed 2d 607, wherein the only recorded instrument was the Trust Deed. In addition, there was a Trust Agreement in the nature of a Contract for the Sale of Real Estate and a Promissory Note. In the instant case, the Peabody Trust

Agreement provided for releases for subdivision development (and was therefore a vehicle for providing the funding for payment of the Promissory Note). The Collateral Assignment set forth the security terms in the same way that the Trust Agreement did in *Barringer* v. *Lilley,* supra, and the instruments collectively in the instant cast were identical to the instruments collectively in *Barringer* v. *Lilley,* except for the separate Trust Agreement in the instant case which provided for releases as a vehicle for funding the repayment of the $50,000.00 Promissory Note. The Court in *Barringer* v. *Lilley,* supra, in effect found that the instruments in that case collectively constituted a mortgage:

> "The fact that Tunney gave a note for $85,000.00 and that the declaration of trust recited that it was to secure payment of the note seem to lead irresistibly to the conclusion that the declaration of trust was regarded as a mortgage."
>
> *Barringer* v. *Lilley,* Cir. 9, 96 F.2d 607 at page 612.

The Court in *Barringer* v. *Lilley* commenting upon the recordation of the Trust Deed, 9 Cir. 96 F.2d 607 at page 613 stated:

> "In either case, the record title in the Title and Trust Company would be sufficient to put all persons on notice that Owens, Dinmore, and Mills did not own the property or that it was encumbered."

Cross-appellant cites Sec. 33-412A of the Arizona Revised Statutes as to the invalidity of unrecorded instruments. In this connection, this Court in *Barringer* v. *Lilley,* 96 F.2d 607 at pages 612-613 in construing Sec. 969 of the Revised Code of Arizona 1928 (now 33-412A) stated:

> "This statute protects creditors and innocent purchasers against an unscrupulous or dishonest owner of record in possession . . . If inquiry was made by the

creditors they would have actual notice of the declaration of trust, else how could Owens explain away the record title in the Title and Trust Company."

"It being established that record title was in the Title and Trust Company, it follows that all creditors were creditors with notice of the fact that Owens and his associates were not owners of the tract, at least so far as the record was concerned—which is notice to all the world."

In the foregoing citation from the Barringer case, this Court has interpreted Sec. 33-412A and by implication has approved recordation of the Trust Deed as being sufficient to comply with requirements of Sec. 33-412A and the Court's conclusion in this respect logically follows, because while the above quoted section provides:

". . . conveyances and deeds of trust shall be recorded."

Yet as quoted by Cross-appellant, Arizona Revised Statutes Sec. 33-702 in defining a mortgage provides:

"Every transfer of an interest in property, *other than in trust*, made only as a security for the performance of another act, is a mortgage, . . ." (emphasis supplied)

So that it appears from the foregoing quoted sections of the applicable Arizona statutes the Arizona legislature did not intend that transfers in trust for security purposes be subject to the same recording provisions as mortgages. On the other hand, a conveyance would fall flatly under Sec. 33-412A which clearly requires the recordation of the Trust Deed, with which there was full compliance in the instant case, the Trust Deed having been recorded on July 31, 1956.

As previously stated and as above quoted, the Court has heretofore held in *Barringer* v. *Lilley*, supra, that

". . . record title was in the Title and Trust Company, it follows that all creditors were creditors with notice . . . which is notice to all the world."

The Arizona Supreme Court in *Maricopa Utilities Company* v. *Cline,* 60 Ariz. 209 at page 214, 134 Pac. 2d 156, 158, stated:

"Notice of facts and circumstances which would put a man of ordinary prudence and intelligence on inquiry is equivalent to knowledge of all of the facts a reasonable diligent inquiry would disclose."

The recorded Trust Deed, Exhibit 2, with its Trust file number, 6007, with its reference to the power of the Trustee to mortgage or pledge the trust property, including mortgage it, to itself, would have lead any reasonable inquirer to the instruments contemporaneously executed with the Trust Deed. For the above set forth reasons, the lien of Phoenix Title and Trust Company having been recorded prior to the lien of any other creditor, except Midway Lumber Company, was superior to all liens recorded subsequent to the Trust Deed and the Trustee in Bankruptcy could not avoid it under Sec. 70(c) or 70(e) of the Bankruptcy Act.

Finally, the Court's attention is directed to *Chicago Federal Savings and Loan* v. *Cacciatore,* Illinois Appellate Court, First Dist. 62-1 USTC 83,361. In this case, by an agreement similar to that between Phoenix Title and Trust Company and Peabody, the taxpayer conveyed all of his interest in certain real property to a Trustee, retaining only a right to reclaim the property, which right, under Illinois law, is deemed to be personal property in the same manner as provided for in the Peabody Trust Agreement. (See paragraph X, page 4 of Exhibit 3) The Trustee, subsequent to the time that the United States recorded notice of its tax liens against the settlor of the trust, executed two mortgages. It was held

that the United States' liens could attach only to the rights of the taxpayer settlor of the trust, which are no more than personal property rights and that the subsequently executed mortgages were valid against the prior recorded Federal tax liens. The Court stated:

> "Thus, state law controls over our conclusion as to the nature of the taxpayer's legal interest in the property sought to be reached, and federal law becomes our guide only in defining the consequences to be attached to such state-created rights by virtue of the federal lien law."
>
> "We cannot agree with the government in this, when to insure the success of such a policy would, as we have held, require upsetting not only long-established principles of state law but also, perhaps, thousands of real estate titles as well." 62-1 USTC 83, 361; p. 83, 365.

Finally, the Court stated at page 83, 364

> "Experience over many years has shown that a land trust performs many commercially useful purposes. It goes far to obviate the cumbersome nature of real estate transactions when there are multiple owners. In the same circumstance, it can simplify the management and financing of real properties and it is especially useful in the financing and marketing of subdivisions and large scale home or apartment building enterprises. Intolerable delays and sometimes insurmountable legal entanglements may result from the death, incompetency or disappearance of an owner of a fractional interest in land. These, too, can be eliminated by the judicious use of a land trust." 62-1 USTC 83, 361; p. 83, 364

III

AUTHORITIES CITED BY CROSS-APPELLANT

The authorities cited by Cross-appellant on page 13 of his brief are not applicable here for two reasons: first,

they do not involve bankruptcy situations; second, they usually refer to statutory liens which are by nature general; thus, in *United States* v. *Knott,* 298 U.S. 544, an insolvent surety company was placed in the hands of state insurance commissioner for liquidation. The Company on commencing business had deposited securities with the State Treasurer as a "trust fund" where the claimants (who could not become known until there had been a default on the part of the company) were not identifiable so that the lien was inchoate. It is quite clear in the instant case that Phoenix Title and Trust Company always was a claimant as distinct from a wide class of possible claimants who were prospective unidentified beneficiaries of a security fund. *United States* v. *Gilbert Associates,* 345 U.S. 361, cited by Cross-appellant is a case involving the priority of Federal taxes over municipal taxes. Bankruptcy was not involved; this was a proceeding under the Federal Insolvency Statutes where the doctrine of choateness of lien determined the superiority of the general tax lien of the Federal government over the general tax lien of the municipality. *United States* v. *Carroll Construction Company,* 346 U.S. 802, was similar to *U.S.* v. *Gilbert* and is a case where the Federal government's tax lien was held superior to the general tax lien of the State of Washington, again by application of the doctrine of choateness of lien under the Federal Insolvency Statutes. *United States* v. *Texas,* 314 U.S. 480, again involved a statutory gasoline tax lien, which lien by statute applied to "all the property of any distributor used in his business"; here the gasoline tax in an insolvency situation was held inchoate for failure to describe in particular the property, subject of the lien, which, of course, is not the situation with Phoenix Title and Trust Company's mortgage lien where the property is particularly described in the Collateral Assignment

and Trust Deed. In *United States* v. *Scovil,* 348 U.S. 218, a landlord's lien was held inferior to a Federal tax lien in an insolvency procedure, representing again a lien against property generally as distinct from property specifically. *United States* v. *Colotta,* 350 U.S. 808, *United States* v. *White Bear Brewing Co.,* 350 U.S. 1010, are two of a series of cases wherein the United States Supreme Court has held mechanic's liens (because they require court proceedings to enforce them) inchoate until judgment is rendered; similary, *United States* v. *Vorreiter,* 355 U.S. 15. None of the cases cited by Cross-appellant involves a bankruptcy situation and the Federal tax liens concerned all deal with general statutory liens inchoate under the Internal Revenue Code. The other cases cited on page 13 of Cross-appellant's brief simply establish the general rule; thus, in *General Motors Acceptance Corporation* v. *Collier,* 106 F.2d 584, it was held that an unrecorded chattel mortgage of an automobile was not prior to the claim of interim creditors giving credit prior to the time that the mortgage was recorded. Similarly, the Sampsell case (*Bank of America* v. *Sampsell,* 114 F.2d 211) wherein it was held an automobile chattel mortgage executed in August 1938 and not recorded until January of 1939 was invalid against an interim bankruptcy. The only case of assistance cited by Cross-appellant is *Joseph* v. *Winakur,* CCA 4, 30 F.2d 510. Here a bill of sale absolute on its face was used as a mortgage and it was held that a failure to record a contemporaneous consignment agreement was fatal under the Mayland statutes which provided:

> "1. Every deed conveying real estate or chattels . . . intended only as security in the nature of a mortgage, though it be an absolute conveyance on terms . . . shall be considered as a mortgage and the person for whose benefit such deed shall be made shall not have any benefit . . . from the recording thereof,

unless every instrument in writing operating as a defense of the same . . . be also therewith recorded." 30 F.2d 510, 513.

This case takes a position opposite from *Barringer* v. *Lilley,* supra. But it will be noted that in that case the Maryland statute *specifically required the recording of all instruments involved in a security transaction,* whereas, under the Arizona statutes it appears that the recording of the Trust Deed is sufficient.

Finally, Cross-appellant on page 16 of his brief quotes the District Court's Order of March 29, 1963 (TR 171) which asserts that the Collateral Assignment (Exhibit 3) of Phoenix Title and Trust Company is no more than an unrecorded chattel mortgage. This contention was answered at length on pages 24-26 of Phoenix Title and Trust Company's Appellant's Brief filed in this cause February 18, 1964, wherein it was established that in defining "mortgageable property the codifiers of the Arizona statutes in adopting the California Code referrable thereto omitted the exception for intangibles."

CONCLUSION

From the authorities set forth above, Cross-appellee, Phoenix Title and Trust Company, respectfully submits that the Bankruptcy Act is complete within itself in establishing priorities and that doctrines and statutory right referrable to the Internal Revenue Code or statutes other than the Bankruptcy Act may not be superimposed upon the Bankruptcy Act in determining the rights of the Trustee in relation to the rights of creditors with liens, and that the security instruments of Phoenix Title and Trust Company, Exhibits 2, 3, 4 and 5, together constitutes a valid mortgage under the doctrine of *Barringer* v. *Lilley,* supra, choate in all respects as defined by the

United States Supreme Court in *United States v. City of New Britain*, 347 US 81 at page 84, and perfected in all respects as heretofore announced by this Court in *Barringer v. Lilley*, supra.

Respectfully submitted,

LOHSE, DONAHUE & BLOOM

By _____

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

NO. 18,819

MYLES STEWART, Trustee of the Estate of ARTHUR PEABODY and OLIVE PEABODY,

Appellants,

vs.

PHOENIX TITLE & TRUST COMPANY,

Appellee.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

LOHSE, DONAHUE & BLOOM

By .....

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IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

PHOENIX TITLE &
TRUST COMPANY,

Appellant,

vs.

MYLES STEWART, Trustee of the
Estate of ARTHUR PEABODY and
OLIVE PEABODY,

Appellees.

No. 18819

ON APPEAL FROM THE UNITED STATES
DISTRICT COURT FOR THE
DISTRICT OF ARIZONA

REPLY BRIEF FOR APPELLEE STEWART

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REPLY BRIEF FOR APPELLEE STEWART

JURISDICTIONAL STATEMENT

This is an appeal from an Order entered on March 29, 1963, by the United States District Court for the District of Arizona affirming the Order of the Referee in Bankruptcy entered May 31, 1962.

This appeal is brought under the jurisdiction established in Section 24 of the Bankruptcy Act, 11 USCA Paragraph 47.

INTRODUCTION

For the sake of clarity, the Phoenix Title & Trust Company, Inc., in its capacity as a creditor of the bankrupt estate will hereinafter be referred to as the "creditor"; the Phoenix Title & Trust Company, Inc., in its capacity as Trustee under the terms of the conveyance by the bankrupts will hereinafter be referred to as the "Trust Company"; all events transpired in Tucson, Pima County, Arizona.

The Transcript of Record will be designated "T.R.", and the Reporter's Transcript will be designated "R.T.".

STATEMENT OF THE CASE

This case grows out of an Involuntary Bankruptcy in which the Bankrupts Peabody had executed four documents:

1. A Deed to Phoenix Title & Trust Company, as Trustee;
2. A Trust Agreement with the Peabodys as beneficiaries and Phoenix Title & Trust Company as Trustee;
3. A Note from the Peabodys to Phoenix Title & Trust Company, creditor, and
4. A Collateral Assignment of the Peabodys' beneficial interest in the Trust Agreement to Phoenix Title & Trust Company, a creditor.

The corpus of the Trust consisted of certain real property and the rights that go with this property. Loss of part of the property and those rights at the time of Bankruptcy had resulted in a cash condemnation award. Said award was not paid until after the adjudication of the Peabodys as Bankrupts.

The Trustee in Bankruptcy and the creditor are disputing the claim made by the creditor that the instruments between the parties are, in effect, a mortgage, and that the recording of the Deed placed the creditor's rights prior in time and security to the Trustee.

It is the Trustee's contention that the Peabodys dealt with Phoenix Title & Trust Company in two capacities, and that the Trustee is prior in time and in security to Phoenix Title & Trust Company, and is therefore entitled to all of the real property and the rights that go with that property as an asset of this Bankrupt Estate. The Referee in Bankruptcy and the District Judge both ruled in favor of the Trustee in Bankruptcy.

FACTS OF THIS CASE

It is pointed out at this early stage of this brief that the "facts" as presented by the creditor-Appellant confuse the issue completely as to the status of "Phoenix Title & Trust Company." All discussions and arguments must of necessity distinguish between Phoenix Title & Trust Company, as Trustee, and Phoenix Title & Trust Company, as creditor. The entire brief of the creditor-Appellant, by attempting to cast Phoenix Title & Trust Company as one entity, rather than a corporation acting in two capacities, is done merely to add weight to the position of Phoenix Title & Trust Company, as creditor, and is a misstatement of fact and law.

An involuntary Bankruptcy Petition was filed against the bankrupt Peabodys on the 15th day of April, 1959. The Peabodys were duly adjudicated bankrupt. The involuntary petition was filed by Ashby Lohse as attorney for William T. Fitchett, Edwin W. Smalley, and Paul E. Greer.

Prior to the filing and adjudication in the involun-

tary proceeding, the Bankrupts and the Trust Company, the Appellant, entered into a transaction described as follows:

> By a recorded Deed, Exhibit 1, Recorder's Transcript, page 136, title to a parcel of real property in Pima County, Arizona, was transferred to the Trust Company, as Trustee. By a separate unrecorded Trust Agreement, Exhibit 1B, the title was held in trust for the Peabodys. The Trustee's Deed was dated July 23, 1956, and acknowledged by the Peabodys on July 26, 1956, was recorded at the request of the Trust Company on July 31, 1956, and duly appears in the records of the County Recorder, Pima County, Arizona. The beneficiaries of the trust are not named in the Trustee's Deed. The Trust Agreement, Exhibit 1B, dated July 23, 1956, was acknowledged by the Peabodys on July 26, 1956, and by officers of the Trust Company on July 31, 1956. Both the Trustee's Deed and the Trust Agreement bear the identification number, "Trust No. 6007."

The Trust Agreement provides that the property to which the Trust Company received title as Trustee (the real property described in the Trustee's Deed, Exhibit 1, which will hereinafter be referred to as the real property), was to be held in trust by the Trustee, the Trust Company, for the beneficiaries, Arthur Peabody and Olive C. Peabody, for the purposes of,

> "subdividing, platting, deeding, selling, conveying, receiving payment for and otherwise handling the property as a whole or in lots and parcels, upon such terms and conditions and for such prices as the Trustee may be instructed in writing so to do by the beneficiaries or their authorized representatives."

Under the provisions of the Trust Agreement, Exhibit 1B, the Trust Company is granted no discretionary

powers and is charged with no responsibility in handling and managing the property. The prescribed duties of the Trust Company are ministerial in nature, to be performed under the direction of the beneficiaries. The settlors, Arthur Peabody and Olive C. Peabody, remained in possession and control of the property and were in possession and control of the property at the time of the bankruptcy herein, with all powers of management, charged with full responsibility for handling the property in carrying out the stated purposes of the trust.

The Trustee's Deed and the Trust Agreement contain no provision that the instruments were executed as security for the performance on the part of the Peabodys of any contract between them and the creditor. There is no reference in the Trustee's Deed or in the Trust Agreement to any other instrument executed or to be executed by the Peabodys as security for the performance on the part of the Peabodys of any contract between them and the creditor.

The Deed to the Trust Company as Trustee and the Trust Agreement were executed by the parties with the intention of establishing a passive depository of the legal title to the real property, with the actual and equitable ownership remaining in the Peabodys for their own use and benefit. The Trust Company as Trustee did not take title to the property as security for the performance of any contract or obligation to be performed on the part of the Peabodys.

On July 24, 1956, the Peabodys made their promissory note, Exhibit 1D, in the principal amount of $50,000.00, payable to the "creditor" on or before July 24, 1957, with interest at the rate of six (6%) per cent per annum from July 24, 1956, interest payable at

maturity. The note recites that it is secured by a collateral assignment, Exhibit 1C, of Peabodys' beneficial interest in Trust No. 6007.

That the "creditor" drew checks payable as follows:

1. Check No. 108, in the amount of $32,701.45, to Arthur Peabody and Olive C. Peabody; for "proceeds of your loan from Phoenix Title & Trust Co."

2. Check No. 107, in the amount of $375.00, to Associated Engineering Co.; for "balance due for cross-sectioning streets in Littletown."

3. Check No. 106, in the amount of $16,712.31, to Valley National Bank; for "payment in full of mortgages from Ackley, DeBand, Kemmeries."

With their note given to the "creditor" on July 24, 1956, the Peabodys, as assignors, executed an instrument designated as "Collateral Assignment of Beneficial Interest" (hereinafter referred to as the assignment) wherein the "creditor" is named as assignee. The assignment bears undated endorsements signed by officers of the "creditor," whereby the "creditor" approves and accepts the assignment as assignee and accepts the assignment as Trustee. The assignment was acknowledged by the Peabodys on July 26, 1956, but was never recorded.

That the Exhibits 1 (deed), 1B (Trust Agreement), 1C (Collateral Assignment), and 1D (note) do not constitute an assignment passing legal title to the "creditor," nor a present assignment of a beneficial interest in property. Furthermore, Exhibit 1 is not a mortgage.

The Collateral Assignment refers to the promissory note for $50,000.00, given by the Peabodys to the "creditor" on July 24, 1956, and provides that for the purpose of securing payment of said note, the assignor does thereby assign, convey, transfer and set over unto the assignee all of his rights, powers, privileges, proceeds and avails of the beneficiary created or reserved, and all of the interest of the beneficiary in Trust No. 6007, insofar as the real property is concerned. The "assignment" contains release clauses in relation to said property, reading as follows:

> "It is provided that the lots into which the property is subdivided may be released by assignor upon the payment to trustee for the benefit of assignee of the sum of $600.00 per lot, said amount to be applied first to the payment of interest to the first of the month next succeeding the date when such funds are available for distribution to assignee and the balance to be applied on (the) principal.
>
> "It is further provided that in the event that the assignor herein has set up a sales escrow in the Phoenix Title and Trust Company that trustee will be authorized to convey a lot or lots to said assignor without the payment of any consideration provided assignor is obtaining a construction loan (including any refinancing, renewal, or increase thereof) from a bona fide lending agency and provided said escrow provides that out of the sales price of said home the escrow agent shall remit the release price and all expenses of sale and conveyance by trustee for such lot or lots to the trustee, it being understood that this amount must be paid not later than the date on or before which the note secured hereby is to be paid in full. The release price herein referred to is the amount of $600.00 per lot as herein set forth."

The "assignment" also provides in the event of

default on the part of the Peabodys in the payment of their note or any of the terms of the assignment that

> "the whole amount of the principal sum and any amount advanced by the assignee . . . shall be . . . deemed to have become due and the same . . . shall be collectible in a suit at law or by foreclosure . . . *as if this collateral assignment of Beneficial Interest were a mortgage. . . .*"
> (Emphasis supplied)

The assignment further provides for the appointment of a receiver "to take charge of said Beneficial Interest and said property."

A notice of tax lien against the Peabodys in favor of the United States of America, dated August 27, 1957, for $4,268.21, was filed August 28, 1957, fee No. 52633, in the office of the County Recorder of Pima County, Arizona.

A notice of tax lien against the Peabodys in favor of the United States of America, dated September 19, 1957, for $2,076.67, was filed September 21, 1957, fee No. 57827, in the office of the County Recorder of Pima County, Arizona.

The only documents recorded or filed in the office of the Pima County Recorder, or elsewhere in Arizona, as evidence of the agreement between the bankrupt and Phoenix Title & Trust Company, as Trustee, or Phoenix Title & Trust Company, the "creditor," was the Deed mentioned as Exhibit 1.

On December 12, 1958, the "creditor" brought an action against the Peabodys and others alleging, in substance, that the Peabodys had given the "creditor" their note for $50,000.00 on July 24, 1956, and in anticipation thereof, and as part of the same transaction, in order to secure the payment of said note, the

parties made and executed the Trust Agreement wherein the Peabodys were beneficiaries and the Trust Company was Trustee under Trust No. 6007; that with the delivery of said note as part of the same transaction, in order to secure the payment of said note, the Peabodys executed and delivered to the "creditor" the assignment of all their beneficial interest in and to all the assets held by the Trust Company under Trust No. 6007; that the Peabodys had defaulted upon the note and assignment under the Trust securing said note; that the sum of $42,536.24, with interest from October 1, 1957, was then due. The complaint demanded, among other things, the following relief:

> "For judgment against Arthur Peabody and Olive C. Peabody, husband and wife, and Paul E. Greer and Evelyn C. Greer, in the sum of $42,536.24 together with interest as provided in said note from October 1, 1957, until paid for plaintiff's attorney fees in a sum equal to ten (10) per cent of all sums found due to date of judgment.
>
> "That the respective *collateral assignments* of defendant Arthur Peabody's and Olive C. Peabody's beneficial interest in the assets of the trust hereinabove referred to be declared to be a first and prior lien against their interest in the property involved, and that said assignments be foreclosed as a mortgage, and the premises therein described and all of said defendants' interest under the terms of said trusts be sold under execution according to the law and practice of this Court to satisfy the demand of the plaintiff. That out of the proceeds of said sale, the plaintiff be paid the amount due; that in case of a deficiency arising from said sale, the plaintiff have judgment for the amount thereof; and that at said sale the plaintiff or any other person to this cause may become purchasers of said premises; that all defendants and all persons or corporations claiming to, under or from

them and all persons having a lien subsequent to said Assignments be forever barred and foreclosed of and from all equity of redemption and claim of, in or to said assigned premises and every part and parcel thereof from and after the delivery of the Sheriff's Deed." (Emphasis supplied)

The action, designated in the docket of said Superior Court as No. 57402, had not been prosecuted to judgment at the time of bankruptcy herein and the case is still pending.

Certain Findings of Fact and Conclusions of Law by the Referee are set forth as they show the Court's Findings of Facts and are repeated here for clarification and amplification.

Finding of Fact II states, in part:

"Under the provisions of the trust agreement the trustee is granted no discretionary powers and is charged with no responsibility in handling and managing the property. The prescribed duties of the trustee are ministerial in nature, to be performed under the direction of the beneficiaries. The trustors, *Arthur Peabody and Olive C. Peabody, remained in possession and control of the property and were in possession and control of the property at the time of the bankruptcy herein,* and with all powers of management, charged with full responsibility for handling the property in carrying out the stated purposes of the trust." (Emphasis supplied.)

Finding of Fact IV states:

"The deed to Phoenix Title as trustee and the trust agreement were executed by the parties with the intention of establishing a passive depository of the legal title to the real property, with the actual and equitable ownership remaining in the Peabodys for their own use and benefit. *Phoenix Title did not take title to the property as security for the performance of any contract or obligation to be performed*

on the part of the Peabodys." (Emphasis supplied.)

Conclusion of Law No. 7 states:

"At the time the notice of each of the federal tax liens was filed as provided in Section 6323 of the Internal Revenue Act of 1954, and at the time of bankruptcy herein, Phoenix Title had *no right in the corpus of Trust No. 6007* as a mortgagee, pledgee, purchaser or judgment creditor." (Emphasis supplied.)

Conclusion of Law No. 8 states:

"At the time the notice of each of the federal tax liens was filed as provided in Section 6323 of the Internal Revenue Act of 1954, and at the time of bankruptcy herein, Phoenix Title had no right in the beneficial interest of the Peabodys in Trust No. 6007 as a mortgagee, pledgee, purchaser or judgment creditor."

Conclusion of Law No. 16 states:

"The real and personal property, title to which is in the name of Phoenix Title by virtue of the deed and trust agreement establishing Trust No. 6007, were assets of the Peabodys at the time of bankruptcy herein and are now assets of the estate of said bankrupts and should be administered by the bankruptcy trustee in these proceedings."

STATUTES INVOLVED

Arizona Revised Statutes:

Section 1-215(22)
Section 33-412A
Section 33-702
Section 33-751(2)
Section 33-753(a)

Internal Revenue Code of 1939:

Section 3672(a)

Internal Revenue Code of 1954:

Section 6323

26 U.S. Code:

Section 6321
Section 6322 (formerly Section 3671)

United States Bankruptcy Act:

Section 70(c)
Section 70(e)

AUTHORITIES

1A Bogert, Trusts and Trustees, Section 206.
90 C.J.S., Trusts, Section 178.
Collier on Bankruptcy, Section 70.45 through Section 70.55.

QUESTIONS PRESENTED

1. Is the lien of Phoenix Title & Trust Company, creditor, voidable under Sec. 70(c) of the Bankruptcy Act?

   (a) Is the Trust Agreement between the Bankrupts Peabody and Phoenix Title & Trust Company an active or passive trust?

   (b) If passive, is it executed by the Statute of Uses?

   (c) If active, was there an equitable conversion which required Phoenix Title & Trust Company to file the instruments as a chattel mortgage?

   (d) Did the failure of Phoenix Title & Trust Company to file the trust deed render it void as to creditors and, therefore, the Trustee-Appellant?

2. Is the lien of Phoenix Title & Trust Company, creditor, inchoate and void as to the United States Government, and therefore as to the Trustee under Sec. 70(c) of the Bankruptcy Act and Sec. 6323 of the Internal Revenue Code of 1954?

ARGUMENT
AN INCHOATE LIEN

In *United States v. R. F. Ball Construction Company,* 78 S.Ct. 443, 355 U.S. 587 (1958), the Court said, "The instrument involved being inchoate and unperfected, the provisions of Sec. 3672(a) of the Revenue Act of 1939 do not apply." The "instrument" in question was an imperfect assignment. It follows in this case that the transaction between the Bankrupt Peabodys and Phoenix Title & Trust Company, as a creditor, if inchoate, results in the Federal tax lien under Revenue statute 6323 to be prior in time and in security to the lien of the creditor, and therefore, the Trustee is prior under Sec. 70(c) of the Bankruptcy Act.

It is the contention of the Trustee that the creditor's lien was inchoate and unperfected by any of the following tests:

(a) The identity of the lienors was not fixed (because the lien was secret for lack of recordation). *United States v. Knott,* 298 U.S. 544, 56 S.Ct. 902 (1936).

(b) Neither title nor possession was in the "creditor." *United States v. Gilbert Associates,* 345 U.S. 361 (1953); *United States v. Carroll Construction,* 346 U.S. 802 (1953), reversing 249 P.2d 234.

(c) The "identification" of the property subject to the lien was not specific and consistent, *United States v. Texas,* 314 U.S. 480 (1941), for the reason that parcels could be released and the lien was not recorded, if the "creditor's" claim is made on the collateral assignment for the reason it was not recorded. The Court is referred to: *United States v. Scovil,* 348 U.S. 218 (1955), reversing 78 S.E.2d 277; *United States v. Colotta,* 350 U.S. 808 (1955), reversing 79 So.2d 474; *United States v. White Bear Brewing Co.,* 350 U.S. 1010 (1956), reversing 227 F.2d 359; *United States v. Vorreiter,* 355 U.S. 15 (1957), reversing 307 P.2d 475.

These cases and the *Ball* case certainly render any lien the Title Company might have inchoate and not subject to the protection given to a ". . . mortgagee, pledgee, purchaser or judgment creditor . . ." in Par. 6323 of the Internal Revenue Code.

As the dissent says in the *Ball* case, at page 445, re Sec. 3672(a), that section does not define the term "mortgagee" and hence we must assume that it was there used in its ordinary and common law sense. Certainly in the case at bar, a Deed to a Trustee or a Collateral Assignment of a Beneficial Interest are not a mortgage in the "common law sense." See also *Beeghly v. Wilson,* 152 F. Supp. 726 (D.C. Iowa 1957).

Interests of "mortgagees" do not force a less demanding test of perfection than do other interests when competing with Federal liens. "We reject the contention that the choateness rule has no place when a 'mortgage' under Sec. 6323 (a) is involved." *United States v. Pioneer American Insurance Co.,* 357 S.W.2d 653 (Ark. 1962),

cert. granted 371 U.S. 909, 83 S.Ct. 254, 9 L.Ed. 2d 169 (1963).

By Federal statute, liens for taxes owing to the United States arise upon receipt by the collector of the assessment list (U.S. Code, Title 26 Par. 6322, formerly Par. 3671), but they attach only to "property and rights to property" belonging to the taxpayer (6321). To quote a succinct comment by Judge Medina:

> "In adopting this legislation, the Congress did not create property interests on which a lien might be imposed; there is no suggestion that it authorized the federal courts to do so. On the contrary, it took for granted here, as it normally does in the tax law, the vital existence of state laws creating and maintaining various interests. The statute was fashioned to require the courts to determine for federal purposes whether those state-created interests are 'property' or 'rights to property'. That classification of interests is a federal question; the existence of the interests to be federally classified, however, is solely a question of state law." *Fidelity & Deposit Co. of Maryland v. New York City Housing Authority,* 241 F.2d at page 144.

In the instant case it is the bankruptcy which transfers the property and rights to property of the bankrupt taxpayer to the Trustee in Bankruptcy.

There seems to be some question in the minds of the creditor-Appellant that the rights of the Trustee under Sec. 70(c) of the Bankruptcy Act were modified by *Constance v. Harvey,* 215 F.2d 571 (1954). There is no question that the Trustee's rights under Sec. 70(c) of the Bankruptcy Act now must be ascertained as of the date of Bankruptcy. The *Constance* case did modify *Lewis v. Manufacturers National Bank of Detroit,* 364 U.S. 603, 81 S.Ct. 347, 5 L.Ed. 2d 323 (1961). The "strong arm clause" of Sec. 70(c) of the Bankruptcy Act,

without using the doctrine of relating back to prior points in time, does not need to be used by the Trustee in this case as there never was a recording of the creditor's security instrument other than the Deed to the Trust Company as Trustee.

In the instant case the Referee in Bankruptcy based his conclusions on Sec. 70(e) of the Bankruptcy Act, which argument is supported by the cross-Appellant Myles Stewart, Trustee of the Bankrupt Estate, and the United States District Court Judge based his decision on Sec. 70(c) of the Bankruptcy Act. It is respectfully contended that both Sec. 70(c) and Sec. 70(e) of the Bankruptcy Act could be used as the basis of the decision, as well as the Arizona law.

The Court is referred to Sec. 70.45 through Sec. 70.55, Collier on Bankruptcy, for a complete discussion of Sec. 70(c) of the Bankruptcy Act.

The creditor, in his Appellant's Opening Brief, seems to make the argument that because a "Trust Deed" was used and recorded that some special rights attach. It is respectfully pointed out again that the State of Arizona does not have a Trust Deed statute, as does California. The Deed to Phoenix Title & Trust Company, as Trustee, was recorded in accordance with Arizona Revised Statute Sec. 33-412(a), which reads as follows:

> "Invalidity of unrecorded instruments as to bona fide purchaser or creditor.
>
> A. All bargains, sales, and other conveyances whatever of lands, tenements and hereditaments, whether made for passing an estate of freehold or inheritance or an estate for a term of years, and deeds of settlement upon marriage, whether of land, money or other personal property, and deeds of trust and mortgages of whatever kind shall be void as to creditors and subsequent

purchasers for valuable consideration without notice, unless they are acknowledged and recorded in the office of the county recorder as required by law, or where record is not required, deposited and filed with the recorder."

We admit the Deed was recorded. The fact of recording adds nothing of value to the argument that the Deed is a "Trust Deed."

Arizona Revised Statutes Sec. 33-702 reads as follows:

"Mortgage defined; pledge distinguished; admissibility of proof that transfer is a mortgage.

"Every transfer of an interest in property, other than in trust, made only as a security for the performance of another act, is a mortgage, except a transfer of personal property accompanied by an actual change of possession, which is deemed a pledge. The fact that a transfer was made subject to defeasance on a condition, may, for the purpose of showing that the transfer is a mortgage, be proved except against a subsequent purchaser or encumbrancer for value and without notice, notwithstanding that the fact does not appear by the terms of the instrument."

This section specifically says, "Every transfer . . . *other than in trust* . . . is a mortgage." This section states the Deed to a Trustee is not a mortgage and *cannot* be foreclosed as one.

A recent Arizona case, *Bank of Arizona v. Harrington, et al.*, 74 Ariz. 297, 248, P.2d 859 (1952), reviews the law on recording and creation of security interests and liens. The Court holds, at page 862, that "A prior unrecorded conveyance or mortgage creates no right as against creditors who have obtained liens." In this case the Deed is not a security instrument. The other instruments were not recorded. The recording of the United States Tax Lien places the United States and the Trustee ahead of the Title Company.

The United States Congress in enacting Sec. 6323 of the Revenue Act intended to give effect to the recording statutes of the several states. The courts must, therefore, give effect to the state recording requirements. *Reiter v. Kille,* 143 F. Supp. 590 (D.C., Pa. 1956).

The effect of the Arizona law would be to place the Bankruptcy Trustee and the United States Tax Lien ahead of the creditor-Appellant.

The priority of lien is governed by the common law rule, "The first in point of time is the first in right." *United States v. City of New Britain,* 347 U.S. 81, 85, 74 S.Ct. 367, 370, 98 L.Ed. 520 (1954).

In conclusion, it would appear the Title Company had "no prior recorded lien" and the circumstances were such that the unrecorded collateral assignment, Exhibit 1C, was not such an instrument that would come under the "*Windsor Square*" case and that the Trust Agreement, Exhibit 1B, was itself not a security device.

"COMMENTS ON

BARRINGER V. LILY

IN RE WINDSOR SQUARE DEVELOPMENT, INC."

Barringer v. Lily, in re Windsor Square Development, Inc., 96 F.2d 607, 9th CAA is cited by Title Company as being "almost identical" with the instant case and therefore controlling. The differences are set forth in what this writer thinks is in order of importance as quoted from the decision of the Court.

(a) "The *Trust instrument* declared that the indebtedness secured thereby (the $85,000 note) was a first lien upon and was secured by the entire beneficial interest thereunder, page 608.

(b) "A *warranty deed* to the property was executed by Mrs. Barringer in favor of Phoenix Title & Trust Company," page 608.

(c) "The fact that Tunney gave a note for $85,000 *and that the declaration of trust recited that it was to secure payment* of the note seem to lead irresistibly to the conclusion that the declaration of Trust was regarded as a mortgage," page 612.

(d) "If inquiry was made by the creditors they would have actual notice of the declaration of trust," page 613.

(e) "Record title was in the title and trust company." This, of course, is not the case in this appeal and the record title was in Phoenix Title & Trust Company, as Trustee, and for no other purposes. The Deed, which the Court construed as a mortgage, was a Deed to a creditor, and not to a Trustee.

The "*Windsor Square Case*" stands for the rule that persons such as those in that case *who have actual notice* are bound by a *declaration of trust* as though all formalities had been complied with, but "As to other persons, without notice thereof, it was as much a nullity as if it had never existed". (96 F.2d at 613·) The Bankruptcy Trustee is such a person without notice.

Although the above should dispose of and completely differentiate the *Windsor Square Case* from the instant case, the writer cannot fail to point out that a reading of the case shows the parties in that case were operating under ". . . circumstances to arouse suspicion," 96 F.2d at 613, and were self dealing.

STATUTE OF USES

In the Findings of Fact and Conclusions of Law dated the 31st of May, 1962, the Referee in Bankruptcy

found, *inter alia,* that Phoenix Title & Trust Company, as Trustee, was granted no discretionary powers and had no responsibility in handling and managing the subject property of the Trust; that the Trustee could act only at the direction of the beneficiaries; that the Deed to the Trustee and the Trust Agreement (Exhibits 1 and 1B, respectively), were executed by the parties with the intention of establishing a passive depository of the legal title to the real property with the actual and equitable ownership remaining in the Peabodys for their own use and benefit; and that Phoenix Title & Trust Company did not take title to the property as security for the performance of any contract or obligation to be performed on the part of the Peabodys. (See Findings of Fact No. II and No. IV, *supra.*)

The District Court, in its Order on Review dated the 29th of March, 1963, upheld the Findings of the Referee and determined that *ipso facto* the Trust was passive and executed by the Statute of Uses. This Court is bound by the decision of the lower court and should not set it aside unless clearly erroneous. *Tepper v. Chichester,* 285 F.2d 309 (9th Cir. 1960).

It is contended by the Appellant that under Sec. 131 of the Restatement of Trusts, admittedly the law in Arizona, the interest of the beneficiaries was personal property and therefore not subject to the operation of the Statute of Uses. This section provides:

> "Restatement of Trusts, Sec. 131 Equitable Conversion.
>
> "(1) If real property is held in trust and by the terms of the trust a duty is imposed upon the trustee to sell it and hold the proceeds in trust or distribute the proceeds, the interest of the beneficiary is personal property."

A further reading of the Restatement will reveal Comment C to this section which provides:

> "*No duty to convert.* The rules stated in this section are not applicable if the trustee has not a duty to convert but merely has a power which he may exercise in his discretion."

In the instant case the Appellant-Trustee did not even have a discretionary power to convert the realty, but could only act upon such terms and conditions as instructed by the beneficiaries in writing. To effect an equitable conversion in a Trust Agreement of realty, the duty must be unconditional and capable of being exercised at any and all times. *Gallagher v. Drovers Trust & Savings Bank,* 404 Ill. 410, 88 N.E.2d 870 (1949); see *In Re Good's Will,* 304 N.Y. 110, 106 N.E.2d 36 (1952); *Rubin v. Bartel,* 371 Ill. 117, 20 N.E.2d 80 (1939); *In re Hencke's Estate,* 212 Minn. 407, 4 N.W.2d 353 (1942). There is a distinction between a duty to sell and a mere authorization to sell on the part of the Trustee, and if the latter, the doctrine of equitable conversion has no application. See *Bitzer v. Moock's Executor and Trustee,* 271 S.W.2d 877 (Ky. 1954). There being no duty to convert on the part of the Trustee, it is manifest that the interest of the beneficiaries remained personalty.

This is true notwithstanding Paragraph X of the Trust Agreement (Exhibit 1B), which provides that

> "The interest of the Beneficiaries in this Trust is personal property, and the Beneficiaries have not and shall not at any time have any right, title or interest in or to the property covered hereby. . . ."

In *Smith v. Bank of American National Trust & Savings Association,* 14 Cal. App. 2d 78, 57 P.2d 1363 (1936), the Court, in dealing with a situation similar to this, held that words in a trust agreement providing that the

beneficiaries' interests should be personalty, and that no beneficiary should have any right, title or interest in and to the property covered thereby, did not create conversion of realty to personalty.

The Appellant further contends, in the alternative, that if the interest remaining in the beneficiaries is real property, the Statute of Uses does not operate thereon because the Trust imposes affirmative duties on the part of the Trustee. This contention is without merit for the power of control, disposition and sole use lies in the beneficiaries, the Appellant being a mere passive depository for the bare legal title. See generally 90 C.J.S. Trusts, Sec. 178.

A trust should not be required merely to accomplish a passing of ownership. 1A Bogert, Trusts and Trustees, Sec. 206. Under the terms of the Trust Agreement (Exhibit 1B) the beneficiaries were to pay all claims, demands, liens, taxes and assessments. The duties of the Trustee served no purpose that could not equally be served without the Trust. Such Trust is held to be simple, passive or dry. 90 C.J.S., Trusts, Sec. 178; see *Elvins v. Seesledt,* 141 Fla. 266, 193 So. 54, 126 A.L.R. 1001 (1940).

Appellant relies heavily on the language in *Chicago Title & Trust Co. v. Mercantile Trust & Savings Bank,* 300 Ill. App. 329, 20 N.E.2d 992. This case is readily distinguished from the instant proceedings in that the Illinois Court found the subject trust agreement sufficient to transfer the beneficial interest under the doctrine of equitable conversion. Upon the foregoing authority, such a conclusion cannot be reached based on the terms of the said Exhibit 1B. Furthermore, the court found the Trustee had a ". . . positive active duty . . . to sell any property remaining in the trust at the end of its prescribed

term. . . .", Id., 20 N.E.2d at 996. Paragraph XIV of the Trust Agreement herein permits the Trustee to convey to the beneficiaries any property not yet conveyed at the termination of the Trust. This does not constitute an active duty within the contemplation of the *Chicago Title* case.

The foregoing notwithstanding, if the interest of the beneficiaries is deemed personal property or that the Trust is active, it would appear as held by the District Court that the Collateral Assignment constitutes an unfiled chattel mortgage, void as to subsequent creditors of the Peabodys. A.R.S. Sec. 33-751(2), Sec. 1-215(22), and Sec. 33-753(1).

THE SCOPE OF REVIEW

The Referee's Findings of Fact and Conclusions of Law (T.R. 123) dealt with mixed questions of law and fact, and he made certain determination on those issues which were affirmed by the United States District Court (T.R. 171).

The Ninth Circuit Court of Appeals in *Tepper v. Chichester,* 285 F.2d 309 (1960), has held at page 312,

> "On review by this Court, we are required to accept the referee's findings unless they are clearly erroneous. Phillips v. Baker, 5 Cir., 1948, 165 F.2d 578; Porterfield v. Gerstel, 5 Cir., 1957, 249 F.2d 634; In re Gerber, 9 Cir., 186 F. 693. In reclamation proceedings, the findings of the referee on questions of intent, purpose, possession and the nature of the dealings between the parties are questions of fact, or in some instances, mixed questions of law and of fact, and the findings of the referee as approved and confirmed by the District Judge will not be set aside on anything less than a demonstration of clear mistake in applying the law. Kowalsky v. American Employers Insurance Co., 6 Cir., 1937, 90 F.2d 476; First National Bank of Portland v.

Dudley, 9 Cir., 1956, 231 F.2d 396; 4 Collier on Bankruptcy, 14th Ed., par. 70.39."

There certainly is in this case a dispute as to facts and it is respectfully submitted that as to those facts the findings of the Referee on questions of intent, purpose, possession, and nature of dealings should be affirmed, and that the District Judge be affirmed.

CONCLUSION

The argument as presented and the law relating to the facts of this action seem clear to the Appellee Trustee in Bankruptcy.

It is respectfully submitted that the entire argument of the creditor is based upon an attempt to distort the facts and the laws of the State of Arizona, and that a clear, simple reading of the Bankruptcy Act and the laws of the State of Arizona should result in the judgment of the Referee in Bankruptcy in the United States District Court being affirmed.

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APPENDIX

United States Bankruptcy Act:

Section 70(c).

The Trustee may have the benefit of all defenses available to the bankrupt as against third persons, including statutes of limitation, statutes of frauds, usury, and other personal defenses; and a waiver of any such defense by the bankrupt after bankruptcy shall not bind the trustee. The trustee, as to all property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt could have obtained a lien by legal or equitable proceedings at the date of bankruptcy, shall be deemed vested as of such date with all the rights, remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such a creditor actually exists.

Section 70(e).

(1) A transfer made or suffered or obligation incurred by a debtor adjudged a bankrupt under this Act which, under any Federal or State law applicable thereto, is fradulent as against or voidable for any other reason by any creditor of the debtor, having a claim provable under this Act, shall be null and void as against the trustee of such debtor.

(2) All property of the debtor affected by any such transfer shall be and remain a part of his assets and estate, discharged and released from such transfer and shall pass to, and every such transfer or obligation shall be avoided by, the trustee for the benefit of the estate: *Provided, however,* That the court may on due notice order such transfer or obligation to be preserved for the benefit of the estate and in such event the trustee shall succeed to and may enforce the rights of such transferee or obligee. The trustee shall reclaim and recover such property or collect its

value from and avoid such transfer or obligation against whoever may hold or have received it, except a person as to whom the transfer or obligation specified in paragraph (1) of this subdivision e is valid under applicable Federal or State laws.

Internal Revenue Code of 1954:

Section 6323. Validity Against Mortgagees, Pledgees, Purchasers, and Judgment Creditors.

(a) Invalidity of Lien Without Notice. Except as otherwise provided in subsection (c), the lien imposed by section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the Secretary or his delegate.

(1) Under State or Territorial Laws. In the office designated by the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law designated an office within the State or Territory for the filing of such notice; or

(2) With Clerk of District Court. In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State or Territory has not by law designated an office within the State or Territory for the filing of such notice; or

(3) With Clerk of District Court for District of Columbia. In the office of the clerk of the United States District Court for the District of Columbia, if the property subject to the lien is situated in the District of Columbia.

(b) Form of Notice. If the notice filed pursuant to subsection (a) (1) is in such form as would be valid if filed with the clerk of the United States

district court pursuant to subsection (a) (2), such notice shall be valid notwithstanding any law of the State or Territory regarding the form or content of a notice of lien.

(c) Exception in Case of Securities.

(1) Exception. Even though notice of a lien provided in section 6321 has been filed in the manner prescribed in subsection (a) of this section, the lien shall not be valid with respect to a security, as defined in paragraph (2) of this subsection, as against any mortgagee, pledgee, or purchaser of such security, for an adequate and full consideration in money or money's worth, if at the time of such mortgage, pledge, or purchase such mortgagee, pledgee, or purchaser is without notice or knowledge of the existence of such lien.

(2) Definition of Security. As used in this subsection, the term "security" means any bond, debenture, note, or certificate or other evidence of indebtedness, issued by any corporation (including one issued by a government or political subdivision thereof), with interest coupons or in registered form, share of stock, voting trust certificate, or any certificate of interest or participation in, certificate of deposit or receipt for, temporary or interim certificate for, or warrant or right to subscribe to or purchase, any of the foregoing; negotiable instrument; or money.

(d) Disclosure of Amount of Outstanding Lien. If a notice of lien has been filed under subsection (a), the Secretary or his delegate is authorized to provide by rules or regulations the extent to which, and the conditions under which, information as to the amount of the outstanding obligation secured by the lien may be disclosed.

26 U. S. Code:

Section 6321. Lien for taxes.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

Section 6322 (formerly Section 3671).
Period of lien.

Unless another date is specifically fixed by law, the lien imposed by section 6321 shall arise at the time the assessment is made and shall continue until the liability for the amount so assessed is satisfied or becomes unenforceable by reason of lapse of time.

Arizona Revised Statutes:

Section 1-215, subdivision 22. Definitions.

22. "Personal property" includes money, goods, chattels, dogs, things in action and evidences of debt.

Section 33-751. Types of personal property which may be mortgaged.

Mortgages may be made upon:

1. All growing crops.

2. All kinds of personal property except on a stock of goods, wares or merchandise daily exposed to sale as set forth in the provisions of § 33-752. As Amended Laws 1956, Ch. 159, § 1.

Section 33-753. Requirements of validity of mortgage.

A mortgage of personal property or crops is void as against creditors of the mortgagor and subsequent purchasers and encumbrances of the property in good faith and for value, unless:

1. The mortgage is acknowledged in like manner as instruments of conveyance of real property.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

.....

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IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

MYLES STEWART, Trustee of the Estate of ARTHUR PEABODY and OLIVE PEABODY,

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INTRODUCTION

For the sake of clarity, the Phoenix Title & Trust Company, Inc., in its capacity as a creditor of the bankrupt estate will hereinafter be referred to as the "creditor"; the Phoenix Title & Trust Company, Inc., in its capacity as Trustee under the terms of the conveyance by the bankrupts will hereinafter be referred to as the "Trust Company"; all events transpired in Tucson, Pima County, Arizona.

OPENING STATEMENT

This brief is submitted in reply to the Brief for the Appellee in the cross appeals between the parties MYLES STEWART, Trustee of the Estate of ARTHUR PEABODY and OLIVE PEABODY, and PHOENIX TITLE & TRUST COMPANY, a creditor.

STATUTES INVOLVED

United States Bankruptcy Act:
Section 64.
Section 67.
Section 70(c).
Section 70(e).

AUTHORITIES

97 Law Ed. 32.

ARGUMENT

Comments on Cases Submitted by the Creditor

In answer to the argument of the Title Company, creditor, that the Bankruptcy Trustee cannot be subrogated to the position of the United States as a creditor under the tax lien laws, a full examination of Section 70(e)(1) and those cases cited by the Title Company, will show that such a statement is not a sound and accurate reporting of the cases cited in the brief of that party, as they relate to the case and issues before this Court.

The following comments on cases cited by the creditor are submitted for the Court's consideration.

1. *In the Matter of F. A. Whitney Carriage Company,* 173 F. Supp. 709 (Nov. 30, 1953).

This case went off on a question of State — *not* Federal — law. The Court ruled, at page 712,

> "I conclude and rule that the mortgage was within the ordinary course of trade and in the regular and usual prosecution of the corporation's business which takes it out from the Massachusetts Statute."

The comments by Sweeney, Chief Judge, in the *Whitney* case as he had ruled (page 711), that Massachusetts General Laws do not make the mortgage complained of "fraudulent," related to the power of a state to determine title to property, not to an issue of priority of recorded versus unrecorded liens.

2. *Silverman v. Wedge,* 158 N.E.2d 668 (1959).

This case is a title case, and Note No. 2 thereof is quoted as follows:

> "The statute is included in c. 63 of the General Laws which deals with excise taxes on corporations. Section 76 and predecessor statutes have always been a provision solely in aid of the collection of such taxes. The earliest form of this statute, St. 1910, c. 187, was entitled 'An Act to prohibit the sale or transfer of the assets of a corporation in fraud of the commonwealth,' and was directed to assisting the collection of taxes imposed by St. 1903, c. 437, esp. §§ 72, 74, historically predecessors of taxes now imposed by G. L. c. 63. The title of an act is to be considered in construing the act. Charles I. Hosmer, Inc. v. Commonwealth, 302 Mass. 495, 501, 19 N.E.2d 800; Rockland-Atlas Natl. Bank of Boston v. Massachusetts Bonding & Ins. Co., Mass., 157 N.E.2d 239. The title corresponded to the narrow scope of the act. It dealt with a special class of taxes and with the Commonwealth as a public body seeking to enforce its taxes. Chapter 187 and § 76 afforded no rights except to the Commonwealth. Failure

to comply with the notice provisions of § 76 gave the Commonwealth alone the power to collect from property, sold otherwise than in the ordinary course of the corporation's business, the taxes then due to the Commonwealth under c. 63. Viewed in context and in the light of its purpose, the statute merely provided to the Commonwealth a tax lien for the particular tax upon the particular property affected, which would be discharged by the payment of that tax by any person. The trustee has and had no duties to perform under the statute. He does not by his mere appointment as trustee represent the Commonwealth. No special benefit is conferred upon him by the statute.

"An amendment of § 76 by St. 1954, c. 461, § 1, changed the wording of the section in a manner which in relevant respects restated the section in language much as it had been interpreted, prior to the amendment, in the Federal case mentioned below, and as we have interpreted the earlier form of the section. See 1 Annual Survey of Mass. Law (1954) 27, 29. 11 U.S.C. (1952) § 110, sub. e(1) [11 U.S.C.A. § 110, sub. e(1)] is not applicable here.

"In a well argued bankruptcy case before the United States District Court for the District of Massachusetts, it was recognized that, even prior to the 1954 amendment, 'the purpose of the statute was . . . to give . . . a lien on property that was transferred without the proper notice' and that the section was not 'intended to cover security transactions' of the type (a mortgage) then before the court."

These above two cases cited as in support of the Title Company, creditor, are actually in support of the Bankruptcy Trustee's position.

The arguments made by the Title Company in reference to the *Sampsell* case, 9 CAA, 1946, 153 F.2d 731, and *In Re Taylorcraft Aviation Corporation,* 168

F.2d 808, are correct statements of law, *but* not applicable to the present case before the Court, and in addition, the statute in question has been amended.

These cases are *priority* cases under Section 64 of the Bankruptcy Act — not *lien* cases under Section 67. In other words, in the *Sampsell* case, "No lien claim was recorded for these taxes," (P. 733, N. 3). The "lien" discussed in this case is the type which arose "by virtue of the fact that the assessment lists of the Commissioner of Internal Revenue." This is true in the *Taylorcraft* case. This is not the case before the Court. In the instant case the liens were recorded in Pima County as required by law. Under present statute the assessment would be enough.

In 97 Law Ed. 32 an excellent annotation covering the question before the Court contains the following at page 47:

> "2. In bankruptcy proceedings, Par. 12, In General.
>
> "Section 64(a) of the Bankruptcy Act (11 U.S.C. § 104(a)) in five classes establishes the order or rank or various debts having priority, in advance of the payment of dividends to creditors, to be paid in full out of bankrupt estates. In the fourth class of such debts are 'taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof'; and in the fifth class 'debts owing to any person, including the United States, who by the laws of the United States in (is) entitled to priority.'
>
> "While Rev Stat § 3466 is material in determining whether a claim of the United States is based on a debt owing to any person who by the laws of the United States is entitled to priority within the meaning of § 64(a)(5) of the Bankruptcy Act, § 3466 is inapplicable in a bankruptcy proceeding for determining the rank or order of the priority of

a claim of the United States as against the claim or interest of others in the bankrupt estate. This question of rank or order is exclusively controlled by the provisions of § 64(a) of the Bankruptcy Act. Re Knox-Powell-Stockton Co. (1939, CA9th Cal) 100 F.2d 979, 38 Am Bankr NS 766; United States v. Sampsell (1946, CA9th Cal) 153 F.2d 731; Re Taylorcraft Aviation Corp. (1948, CA6th Ohio) 168 F.2d 808; Adams v. O'Malley (1950, CA8th Neb) 182 F.2d 925, infra; Re L. E. Elliott Brokerage Co. (1942 DC Kan) 48 F. Supp. 144; Re Van Winkle (1943, DC Ky) 49 F. Supp 711, 53 Am Bankr NS 296. But see United States v. Reese (1942, CA7th Ill) 131 F.2d 466, 51 Am Bankr NS 660, infra.

"In determining the priorities under the Bankruptcy Act, Rev Stat § 3466 is not even useful by way of analogy as it sets up an all-over priority without exception, while the Bankruptcy Act has its own schedule of priorities intended to cover all situations within its terms and jurisdiction. United States v. Sampsell (1946, CA9th Cal) 153 F.2d 731.

"Under the Bankruptcy Act, as amended in 1926, debts due the United States are given priority under § 64, but lien creditors come under § 67 (11 USC § 107), and are prior in right to taxes without a lien under § 64. Id.

"The rule, established in nonbankruptcy proceedings, that an inchoate lien will not defeat the priority established by Rev Stat § 3466 is not applicable in bankruptcy proceedings. Re Knox-Powell-Stockton Co. (1939, CA9th Cal) 100 F.2d 979, 38 Am Bankr NS 766 (giving priority to prior state tax liens over a tax claim of the United States); United States v. Sampsell (1946, CA9th Cal) 153 F.2d 731 (holding that the United States was not entitled to priority in payment for gasoline taxes out of a bankrupt's estate, over a state's claim for franchise taxes and a mortgagee's claim for interest and attorney's fees relating to its mortgage).

"Under § 64(a) of the Bankruptcy Act inchoate tax liens in favor of the United States (for withholding and social security taxes) were held to be on a parity with inchoate county tax liens (for personal property taxes), and Rev Stat § 3466, was held not to be applicable so as to give the federal liens priority over the county liens, in Adams v. O'Malley (1950, CA8th Neb) 182 F.2d 925. At the time of the adjudication, the property of the bankrupt was subject to liens for unpaid personal property taxes levied by the county by virtue of state law, and to liens for unpaid federal taxes by virtue of federal law. Neither the state nor the United States had at that time foreclosed its liens or levied upon any specific property of the bankrupt. The decision was rested on the ground that the Bankruptcy Act provides a complete and exclusive system for administering and distributing the estates of bankrupts, and that under § 64(a) of the Bankruptcy Act taxes legally due and owing by the bankrupt to the United States and taxes due to any state or any subdivision thereof are on a parity. The question as to whether the United States should be given priority because its liens were specific and perfected, while those of the county were general and inchoate, was left open as unnecessary to determine, since the statutory liens of the county were no more general and inchoate than were the liens of the United States; and, if a seizure was a prerequisite to the perfection of the county's liens, they were held perfected after bankruptcy by the filing of notice with the court as permitted by § 67(b) of the Bankruptcy Act (11 USC § 107(b)).

"Inconsistent with the authorities referred to above is United States v. Reese (1942, CA7th Ill) 131 F.2d 466, 51 Am Bankr NS 660, where, without considering the effect of the priority provisions of the Bankruptcy Act, the court relied upon Rev Stat § 3466 in support of its holding that a federal tax lien had priority in bankruptcy proceedings

over a state's statutory lien upon real estate for taxes due thereon. In United States v. Sampsell (1946, CA9th Cal) 153 F.2d 731, it was pointed out that United States v. Reese (F) supra, was not controlling because there was a failure in that case to consider the applicable provisions of the Bankruptcy Act and also because that case relied upon authorities which are inapplicable under the Bankruptcy Act."

It is contended by the Title Company that a "Federal tax lien in bankruptcy is nothing more than a general inchoate lien." This may be a correct statement of the law where no recording of the lien has been made. It is plainly incorrect and ridiculous where the lien was recorded prior to adjudication. Again it is pointed out that the statute was amended, and such a lien is valid and subsisting after the assessment list is prepared.

Comments on
"Equity of the Case"

These comments are made in light of what the writer of this brief feels the Ninth Circuit Court considered in the case of *Pacific Finance v. Edwards,* 304 F.2d 224, 9th CAA (1962).

The Ninth Circuit Court appeared to be troubled in the *Pacific Finance Company* case with an attempt by a Trustee to invalidate a "security interest for the benefit of general creditors," which creditors could not attack the transaction the Trustee sought to set aside, and which creditors did not in fact exist. This is *not the situation* before the Court at the present time.

It is interesting to note that the general creditors, most of whom have sought judgment (see pages 4 through 6 of the Appellant Phoenix Title & Trust Company's Opening Brief for a list of creditors and the

dates of their judgments), were in the construction business and furnished materials and labor to the bankrupt for use in connection with the real property in question. It is reasonable to assume that if these general creditors knew of the "secret lien" of the *creditor*, Phoenix Title & Trust Company, these general creditors would have taken steps to protect themselves, or avoid doing business with the bankrupts on any basis.

To allow the general creditors, such as the class of persons who lent money, furnished materials, and generally dealt with the bankrupts, to be deprived of the assets which the Trustee seeks to recover in this action would be an inequity upon the general creditors and not upon Phoenix Title & Trust Company as a creditor.

In *Moore v. Bay,* 284 U.S. 3 (1931), the Supreme Court said that in asserting rights for general creditors, the Trustee does not invalidate "security instruments" for the sole benefit of any single creditor and the distribution of proceeds from such an action is for the distribution of all general creditors. Certainly equity is on the side of general creditors who supplied materials, lent money and supplied the bankrupt builder and developer with the necessary funds to carry on his construction project where a secret lien is trying to be enforced by Phoenix Title & Trust Company, as creditor. All that is asked of the creditor in this case is that he comply with state law in perfecting his security. This means that the creditor only had to give notice to others that certain of the bankrupts' property was subject to its lien. Only if the creditor, Phoenix Title & Trust Company, did not comply with the state laws does the Bankruptcy Act make its avoiding sections, to-wit, Section 70(c) and Section 70(e), applicable to the situations and vest rights in the Trustee in Bankruptcy. If the creditor,

Phoenix Title & Trust Company, insists upon talking about equitable principles, all the Court and that creditor has to remember is that its protection lies in its own hands, and all the creditor had to do was record the Collateral Assignment of the Beneficial Interest from Peabodys to Phoenix Title & Trust Company.

In this particular case it is pointed out again that the Trustee does not need to reach back to a point of time before the time of bankruptcy to invalidate the "security transaction" between Phoenix Title & Trust, as creditor, and the Peabodys under Section 70(c) of the Bankruptcy Act, because the transaction was never altered at a later date by Phoenix Title & Trust Company, as creditor, recording the security instrument, to-wit, the Collateral Assignment of Beneficial Interest.

Even without the authorities of Section 70(c) and Section 70(e) of the United States Bankruptcy Act, the transaction between Phoenix Title & Trust Company, as creditor, and the bankrupt Peabodys was void as to subsequent creditors for the reasons that the "security instrument" of Phoenix Title & Trust Company, a creditor, was never recorded and there was no notice to general creditors.

CONCLUSION

It is therefore respectfully submitted that the decision of the United States District Judge should be confirmed under Section 70(e) of the Bankruptcy Act, and the State laws of Arizona, in addition to the Court's given reasons under Section 70(c) of the Bankruptcy Act.

.....

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APPENDIX

United States Bankruptcy Act:

Section 70(c).

The Trustee may have the benefit of all defenses available to the bankrupt as against third persons, including statutes of limitation, statutes of frauds, usury, and other personal defenses; and a waiver of any such defense by the bankrupt after bankruptcy shall not bind the trustee. The trustee, as to all property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt could have obtained a lien by legal or equitable proceedings at the date of bankruptcy, shall be deemed vested as of such date with all the rights, remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such a creditor actually exists.

Section 70(e).

(1) A transfer made or suffered or obligation incurred by a debtor adjudged a bankrupt under this Act which, under any Federal or State law applicable thereto, is fraudulent as against or voidable for any other reason by any creditor of the debtor, having a claim provable under this Act, shall be null and void as against the trustee of such debtor.

(2) All property of the debtor affected by any such transfer shall be and remain a part of his assets and estate, discharged and released from such transfer and shall pass to, and every such transfer or obligation shall be avoided by, the trustee for the benefit of the estate: *Provided, however*, That the court may on due notice order such transfer or obligation to be preserved for the benefit of the estate and in such event the trustee shall succeed to and may enforce the rights of such transferee or obligee. The trustee shall reclaim and recover such property or collect its

value from and avoid such transfer or obligation against whoever may hold or have received it, except a person as to whom the transfer or obligation specified in paragraph (1) of this subdivision e is valid under applicable Federal or State laws.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

.....

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STATEMENT ON THE FACTS OF THE CASE

Throughout all briefs in this case there has been a difference of opinion between the parties as to the facts. Appellee has stated as a fact the "intention of the parties" in the execution of Exhibits 2 (Deed), 3 (Trust Agreement), 4 (Note) and 5 (Collateral Assignment), but has cited no testimony on this point. Likewise, Apellee has contended the Peabodys were in "possession" to date of bankruptcy whereas Appellant has contended it was in possession at that time. It will serve no purpose to reallege the facts contended by Appellant, so Appellant realleges the facts stated in all its briefs filed in this action, together with its fact citations in support thereof.

ARGUMENT

I

AS RESPECTS APPELLEE'S POSITION IN RE INCHOATE LIEN

The authorities cited by Appellee Stewart on pages 13 and 14 of Appellee's answering brief have heretofore been discussed at length and distinguished on pages 22 to 25 of Phoenix Title's opening brief as Appellant Suffices it to say none of the cases cited by Appellee Stewart pinpoint any particular in which the lien of Phoenix Title & Trust fails for want of choateness. The doctrine of choateness of liens was re-explained last November in *Hammes v. Tucson Newspapers, Inc.*, 324 F.2d 101, when the Court of Appeals for the Ninth Circuit applied the doctrine to the lien of Tucson Newspaper arising out of its assignment of money payments to be received in futuro under a land contract.

At this point it might be well to distinguish between the Trustee in Bankruptcy attempting to determine priority between two competing liens, where one of the liens is a tax lien of the United States Government, and the situation where the Trustee in Bankruptcy is attempting to set aside a lien through the machinery of the Bankruptcy Act under §70(e). In the former situation, bankruptcy is really not involved. The trustee is simply a stakeholder trying to determine which of two competing lien holders is entitled to certain specific assets of the bankrupt. Such a situation is reflected in *Hammes v. Tucson Newspapers, Inc., supra,* where the bankrupty trustee was trying to determine if Tucson Newspapers was entitled to certain assets of the bankrupt, or the Federal Government under its recorded tax liens. In this latter situation where the Bankruptcy Act was not employed to set aside a lien, reference was made to

Federal law to determine the priority of the competing lien of Tucson Newspapers and in that particular case it will be noted that the court found that the recorded assignment of the payments to be received in futuro under the land contract constituted a choate and valid security device and that Tucson Newspapers was a "mortgagee" within the meaning of 26 USC §6323(a). The court also applied the same doctrine in *Hoare v. U.S.*, 9th Cir. 1961, where the situation involved competing liens, and again the security device employed there was determined to be a mortgage within the protection of §6323(a).

Such is not the situation in the instant case. Here the United States Government is not asserting its lien and the bankruptcy trustee is not acting as a stakeholder trying to determine which of two competing lienors is entitled to bankrupt assets. Instead, here the bankruptcy trustee is trying to subrogate himself under §70(e) of the Bankruptcy Act not to establish a priority of one lien over another, but rather to dissolve entirely or set aside the lien of Phoenix Title & Trust Company through §70(e). As previously stated in Phoenix Title & Trust Company's brief as Appellee, page 6, et seq., the doctrine of choateness of lien has been consistently rejected with other sections of the Bankruptcy Act where it was attempted to interpolate that doctrine arising under the Federal Tax Statutes into the machinery of the Bankruptcy Act itself. In any event, assuming that the doctrine of choateness of lien did apply to the operation of the Bankruptcy Act itself, it is clear that under all the tests the lien of Phoenix Title & Trust Company is choate as determined by the District Court in its order March 29, 1963 (TR 171) wherein it reversed the Referee on Conclusions of Law 11 and 13.

In addition, Appellee Stewart in asserting the doc-

trine of choateness of lien inconsistently jumps from federal law to state law in determining whether or not Phoenix Title & Trust Company's trust device is a mortgage. As this court held in *Hammes v. Tucson Newspapers, Inc.*, 324 F.2d 101 (9 Cir.) at page 103:

> "It also held that Tucson Newspapers is a mortgagee within the meaning of 26 U.S.C. §6323(a) which is a federal law question. Again we agree."

This court also held in *Hoare v. U.S.*, 294 F.2d 823 (9 Cir.) at page 825:

> "What is meant by the word 'mortgagee' as used in §6323(a) however is a federal question as to which state law is to be considered but is not controlling."

It is apparent from the foregoing that the doctrine of choateness of lien simply referable to Federal tax liens is not applicable to a case where the machinery of the Bankruptcy Act is being used in an atempt to dissolve an existing lien of a creditor. Where the Bankruptcy Act machinery is being used to set aside a lien, the only question is whether or not the lien of the creditor is valid under state law. The doctrine of choateness of lien applies in bankruptcy situations not where the Bankruptcy Act is involved, but simply where the trustee is a stakeholder attempting to determine between competing liens (one of which is a federal tax lien), which is prior under a situation which does not exist in the instant case.

It is also notable that in *Hammes v. Tucson Newspapers, Inc., supra*, the court found the assignment from Arizona Stores, Inc. to Tucson Newspapers, Inc. of payments to be made in futuro under a land contract constituted a mortgage device within the meaning of §6323(a), showing the wide scope of devices which the court has consistently found, so long as they were for security purposes, to constitute a mortgage within

the contemplation of §6323(a) of the Internal Revenue Code.

Nowhere has Appellee Stewart cited any authority for the proposition that the machinery of the Bankruptcy Act may be invoked by the bankruptcy trustee to clothe the trustee with special powers which apply to a sovereign government as is the situation with the Federal Government and the doctrine of choateness of lien as applicable to federal tax liens. On the other hand, Appellant Phoenix Title & Trust Company has cited two cases directly in point supporting the proposition that §70(e) of the Bankruptcy Act may not be used by a bankruptcy trustee to clothe the bankruptcy trustee with powers which are referable to a sovereign government. These are *Silverman v. Wedge,* 158 N.E. 2d 668, and *In the Matter of F. A. Whitney Carriage Company,* 173 F. Supp. 709. Those cases flatly hold that the bankruptcy trustee may not be subrogated to the special powers referable to a state government. It, therefore, follows that the same principle should apply to the proposition that the bankruptcy trustee may not be subrogated through §70(e) of the Bankruptcy Act to the special powers of the Federal Government.

II

ARGUMENT CONCERNING APPELLEE STEWART'S COMMENTS ON BARRINGER v. LILLEY

Appellee Stewart sets forth on pages 18 and 19 of his answering brief distinctions which he believes exist between *Barringer v. Lilley,* 96 F.2d 607, 9th Cir., from the instant case. The only difference (which is not material) is that in the instant case there were four instruments instead of three. In *Barringer v. Lilley* the court construed the three instruments there involved as

collectively constituting the security device. In the instant case it is Appellant Phoenix Title & Trust Company's position the court should in like manner construe collectively not three but four instruments as constituting the security device. The only significant difference between the two cases is that there exists a Trust Agreement (Exhibit 3) in the instant case, the purpose of which was to provide a vehicle by which sales could be made of lots to provide for funding the payment of the Promissory Note (Exhibit 4) secured by the Collateral Assignment (Exhibit 5). It scarcely seems logical that the existence of one instrument—a trust agreement providing for lot sales as a funding device for payment of the mortgage—should constitute a destruction of the mortgage itself; yet that apparently is the position of Appellee Stewart. The equivalent instruments in the two cases are simply the Declaration of Trust in Barringer which recited the $85,000.00 note and the Collateral Assignment (Exhibit 5) in the instant case, which does the same thing. Certainly, the addition of an additional security device—the Trust Agreement (Exhibit 3) which provides a funding device for payment of the mortgage —should not impair the security. The mere addition of this additional instrument appears to be the sole basis by which Appellee Stewart argues that the doctrine of *Barringer v. Lilley* is inapplicable to the instant case.

III

ARGUMENT CONCERNING APPELLEE STEWART'S COMMENTS ON STATUTE OF USES

Appellee Stewart on pages 19 through 23 of his answering brief in making comments on the Statute of Uses completely ignores Part B of Appellant Phoenix Title's opening brief in which Appellant cites the neces-

sity to construe the instruments creating its lien together. Clearly, if the critical instruments involved in this appeal, the Trust Deed (Exhibit 2), the Trust Agreement (Exhibit 3), the Promissory Note (Exhibit 4) and the Collateral Assignment of Beneficial Interest (Exhibit 5) are construed together, those collective instruments create a security device equivalent to a mortgage and the application of the doctrine of the Statute of Uses is no more pertinent there than it would be with the statutory California trust deed. In any event, the duties of the trustee in enforcing the mortgage are such active duties as to bring the device beyond the purview of the Statute of Uses and it should be noted at this point that a primary basis of Phoenix Title's appeal in this case is the arbitrary refusal of the Referee, sustained by the District Court, to construe the above instruments together, notwithstanding the fact that they were executed and delivered concurrently on July 26, 1956, and not withstanding the legal authorities cited on page 12 of Appellant Phoenix Title's opening brief. Nowhere is there any evidence in the record nor has there been legal authority cited to sustain the Referee's refusal to regard these instruments collectively.

But assuming that the Referee in the District Court may be sustained in this arbitrary division of the instruments involved, first into trust instruments and then into security instruments, it is Appellant Phoenix Title's position that the Statute of Uses has not been executed, but under the cited authorities, including the Restatement of Trusts, Section 131, as cited by Appellee Stewart on page 20, the duties of Phoenix Title & Trust Company as Trustee were positive, affirmative duties at such time as lot sales were made to convey title to the real property sold to the respective purchasers; that these were mandatory duties so that the trust could not, even under this

strained construction of the collective instruments, be a passive trust.

Thus, the Trust Agreement (Exhibit 3) page 1 provides:

> ". . . that the Trustee holds and will hold the title to said property in trust for the purpose of subdividing, platting, deeding, selling, conveying, receiving payment for and otherwise handling the property as a whole or in lots or parcels, upon such terms and conditions and for such prices as the Trustee may be instructed in writing so to do by the Beneficiaries or their authorized representative . . ."

The fair import of the foregoing is that when notified of a lot sale the trustee was under a mandatory duty to convey the lot sold to the purchaser.

The Court is referred to the extensive argument of Appellant, Phoenix Title, in its opening brief, pages 15 to 24.

CONCLUSION

In view of the authorities, facts and arguments set forth above and in Appellant's opening brief, Appellant submits:

1. That the doctrine of choateness of lien as rejected by the District Court is not applicable in a bankruptcy situation except in the situation where the bankruptcy trustee is acting simply as a stakeholder and deciding between two or more competing liens, one of which is a federal tax lien.

2. That the facts of the instant case come within the doctrine of *Barringer v. Lilley, supra,* and that a distinction between that case and the instant case cannot, logically, be predicated solely on the proposition that there

was an extra instrument, to-wit, a trust agreement which simply provided a vehicle for funding the payment of the mortgage by lot sales.

3. That the Referee in District Court erred by failing to construe the critical instruments involved in this appeal together notwithstanding that all evidence showed that they were executed and delivered concurrently on July 26, 1956, and notwithstanding the fact that all existing legal authority provides, in the absence of evidence to the contrary, that the instruments should be construed collectively and together, and if the critical instruments involved in this appeal are construed together, the Statute of Uses simply is not applicable to a situation where the device employed as urged by Appellant, Phoenix Title & Trust Company, is simply a mortgage. On the other hand, if the instruments are not construed together, the affirmative duties of the trust agreement including the duty to convey when lot sales are made reflect an active trust so that the Statute of Uses is not executed. Finally, Appellant urges that the application of the Statute of Uses to terminate the trust should be confined to special situations such as where partition of trust assets is desirable in the case of long inactive trusts as reflected in the cases cited by the District Court and as discussed on page 23 of Appellant's opening brief.

Respectfully submitted,
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By.....
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I certify that, in connection with the preparation of this Brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing Brief is in full compliance with those rules.

.....

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No. 18,825

United States Court of Appeals

For the Ninth Circuit

UNITED STATES OF AMERICA, for the Use and Benefit of Miller & Bentley Equipment Company, Inc.,

Appellant,

vs.

JAMES H. KELLEY (KELLY), UNITED PACIFIC INSURANCE COMPANY, MAURICE RAMAGE and FRED AYALA,

Appellees.

Appeal from the District Court for the District of Alaska

BRIEF OF APPELLANT

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No. 18,825

United States Court of Appeals

For the Ninth Circuit

UNITED STATES OF AMERICA, for the Use and Benefit of Miller & Bentley Equipment Company, Inc.,

Appellant,

vs.

JAMES H. KELLEY (KELLY), UNITED PACIFIC INSURANCE COMPANY, MAURICE RAMAGE and FRED AYALA,

Appellees.

Appeal from the District Court for the District of Alaska

BRIEF OF APPELLANT

JURISDICTIONAL STATEMENT

This is an appeal from a judgment of the United States District Court for the District of Alaska. The judgment appealed from was entered on May 17, 1963. Pursuant to Rule 52(b), on May 22, 1963, appellant filed a motion to amend Findings of Fact and Conclusions of Law and to Make Additional Findings, and on June 21, 1963, the motion was heard and granted in certain respects and denied in others. Notice of Appeal was filed on July 11, 1963.

This Court has jurisdiction of the appeal by virtue of 28 U.S.C.A. 1291.

STATEMENT OF THE CASE

This is an action under the Miller Act, 40 U.S.C. 270(a), against a general contractor and his surety by a supplier of a subcontractor. The case has previously been before this Court, *United States of America for the Use and Benefit of Miller & Bentley Equipment Company, Inc. v. James H. Kelley, et al.*, No. 17,730. Pursuant to order of this Court, the opinion was not published.

On the previous appeal this Court had before it a cross-appeal by the general contractor and his surety from a summary judgment in favor of appellant-supplier. The issues before this Court on the cross-appeal were whether appellant was entitled to rental on equipment furnished to the subcontractor after the subcontract had been terminated (without notice to appellant) and whether appellant gave notice to the general contractor within the period required by law.

On each of these issues this Court stated that "a genuine issue of fact remains to be determined" and accordingly reversed the summary judgment and remanded the issues on the cross-appeal for further proceedings.

In accordance with the directions of this Court a trial on the issues raised on the cross-appeal was held, at the conclusion of which the District Court found

that the subcontract between the general contractor and the subcontractor was terminated on January 12, 1959, "that (appellant), as a reasonable and prudent supplier, should have known on or after February 15, 1959, of the termination of the subcontract and cannot claim to have continued in good faith to believe that its equipment was being used on the job after that date". The District Court further found that on April 28, 1959, appellant gave the general contractor notice of its claim, and that this notice was in compliance with the requirements of the Act. The District Court further found, however, that the 90 day period for giving notice to the general contractor expired on April 11, 1959, that appellant was not diligent "in making its claim", and under the facts and circumstances of the case did not, subsequent to January 13, 1959, furnish any labor or materials in the prosecution of the work under the general contractor's contract with the United States. Accordingly, judgment was granted to defendants.

STATUTE INVOLVED

The Miller Act, 40 U.S.C. 270(b) provides in its pertinent part:

> "(a) Every person who has furnished labor or material in the prosecution of the work provided for in such contract, in respect of which a payment bond is furnished under this Act and who has not been paid in full therefor before the expiration of a period of ninety days after the day

on which the last of the labor was done or performed by him or material was furnished or supplied by him for which such claim is made, shall have the right to sue on such payment bond for the amount, or the balance thereof, unpaid at the time of institution of such suit and to prosecute said action to final execution and judgment for the sum or sums justly due him: Provided, however, *That any person having direct contractual relationship with a subcontractor but no contractual relationship express or implied with the contractor furnishing said payment bond shall have a right of action upon the said payment bond upon giving written notice to said contractor within ninety days from the date on which such person did or performed the last of the labor or furnished or supplied the last of the material for which such claim is made*, stating with substantial accuracy the amount claimed and the name of the party to whom the material was furnished or supplied or for whom the labor was done or performed. Such notice shall be served by mailing the same by registered mail, postage prepaid, in an envelope addressed to the contractor at any place he maintains an office or conducts his business, or his residence, or in any manner in which the United States marshal of the district in which the public improvement is situated is authorized by law to serve summons." (Emphasis supplied.)

SPECIFICATIONS OF ERROR RELIED ON

1. The District Court erred in holding that notwithstanding that appellant, as a reasonable and prudent supplier, knew or should have known on February 15, 1959, that its equipment was no longer on the project, appellant was required to give appellee James H. Kelley notice of its claim under the Miller Act, 40 U.S.C. 270(b) on or before April 11, 1959.

2. The District Court erred in dismissing the action on the grounds set forth in the preceding paragraph.

QUESTION PRESENTED

The question presented on this appeal is whether a supplier, renting equipment and furnishing other labor and materials to a subcontractor on a construction project subject to the Miller Act, who has no notice of the termination of the subcontract by the prime contractor, has ninety days in which to give the required statutory notice of claim to the prime contractor after he knew or should have known his equipment was no longer being used on the project, even though he was "not diligent" in giving the notice of claim. Stated in another way, the question presented is whether a supplier has the full statutory period of ninety days in which to give the required notice despite the fact that had he been "diligent" the supplier would have given notice in less than the ninety days permitted under 40 U.S.C. 270(b).

ARGUMENT

Under the findings of the District Court, appellant, as a reasonable and prudent supplier, should have known on or after February 15, 1959, that the general contractor had terminated the subcontract between him and the subcontractor to whom appellant had been renting equipment used in the performance of the subcontract. Clearly implicit in this Court's previous opinion is that the ninety day period for giving the notice required by the Act does not commence until a reasonable prudent supplier should have known of the termination of the subcontract and that its equipment was no longer being used on the job. Under this view, appellant had ninety days from February 15th—or until May 16th—within which to give the required notice. The District Court expressly found that notice which in form complied with the Act was given on April 28th. This was within the ninety day period, and accordingly satisfied the requirements of the Act.

Nevertheless, the District Court found that after being on notice of the termination of the subcontract appellant was not diligent in giving notice to the general contractor, and for some reason not manifest found that because of this lack of diligence appellant was not entitled to recover. Assuming that the ninety day period commences on the date appellant should have been on notice of the termination of the subcontract, the action of the District Court in imposing a limitation on the ninety day period based on a nebulous standard of diligence amounts to nothing less than judicial abrogation of Congressional enact-

ment. Under the Act appellant had ninety days after whatever date the law establishes as the date upon which the ninety day period commences. This Court having previously stated that the period commenced on the date when appellant knew or as a reasonable supplier should have known of the termination of the subcontract, the notice given by appellant was clearly within the ninety days and therefore satisfied the statutory requirements. cf. *United States v. Endebrock-White Co.,* (4th Cir. 1960) 275 F. 2d 57.

CONCLUSION

For the reasons stated, it is respectfully submitted that the District Court's order dismissing the action be reversed, and the cause remanded for further proceedings.

Dated, Fairbanks, Alaska,
October 7, 1963.

CHARLES E. COLE,
Attorney for Appellant.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

CHARLES E. COLE.

No. 18,825

United States
COURT OF APPEALS
for the Ninth Circuit

UNITED STATES OF AMERICA, for the Use and Benefit of Miller & Bentley Equipment Company, Inc.,

Appellant,

v.

JAMES H. KELLEY (KELLY) and UNITED PACIFIC INSURANCE COMPANY,

Appellees,

and

MAURICE RAMAGE and FRED AYALA,

Defendants.

BRIEF OF APPELLEES

Appeal from the District Court for the District of Alaska

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United States
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MAURICE RAMAGE and FRED AYALA,

Defendants.

BRIEF OF APPELLEES

Appeal from the District Court for the District of Alaska

JURISDICTION

Appellees accept appellant's statement of jurisdiction.

STATEMENT OF THE CASE

Plaintiff's complaint was filed August 19, 1959, seeking judgment against defendants Ramage and Ayala

on contract and against appellees on a Miller Act bond. The District Court decided the case on summary judgment on August 16, 1961, in an opinion reported at 192 F. Supp. 274.

Appellant appealed from that judgment specifying as error the District Court's granting appellees' motions for summary judgment numbered 2 and 8 relating to alleged tractor rentals and labor and material furnished to the tractors in an attempt to make them operable. In its opening brief appellant waived its appeal from the granting of appellees' motions for summary judgment numbered 4, 5, 6 and 7.

This court in its per curiam opinion of February 1, 1963 (Case No. 17,730) affirmed the District Court's granting summary judgment on motions numbered 2 and 8. That judgment thereupon became the law of the case.

Appellees' cross appeal from the original summary judgment resulted in this court reversing the summary judgment in favor of appellant for the sum of $5,726.21. This court had assumed that this judgment was solely "for the rental of equipment (other than that which was the subject of the appeal of appellant) furnished by appellant to the subcontractor at the job site." Based on this *assumption,* the court remanded the case to the District Court to determine whether under all the facts and circumstances the "termination of the subcontract [on January 13, 1959] should have started this [90-day] period running."

On the trial on remand it appeared from the evi-

dence that the only equipment of subcontractor ever used at the job site for the prosecution of the work was the two tractors being purchased under conditional sale contracts which were the subject of appellant's previous appeal. Although the previous appeal had affirmed the District Court's granting of summary judgment on appellees' motion number 8 and had precluded appellant from recovering for materials allegedly furnished in an effort to make these two tractors operable, it appeared on remand that virtually the entire amount of appellant's remaining claim consisted of labor and materials and certain rented items used away from the job site exclusively in an attempt to make the conditional sale tractors operable.

The two tractors, of course, never were capable of performing the required work. The subcontract with defendants Ramage and Ayala was entered into on October 22, 1958, and provided for completion no later than January 1, 1959. When the subcontract was terminated and the two tractors removed from the job site on January 13, 1959, scarcely half the work had been performed. Appellee Kelley, using one tractor of his own (smaller in size than either of the two tractors attempted to be used by the subcontractors), completed the remaining work in approximately three weeks.

Based on the record of appellant's case alone the District Court found that:

> "Under the facts and circumstances of this case, plaintiff did not, subsequent to January 13, 1959, furnish any labor or materials used in the prosecution of the work provided for under defendant

Kelley's contract with the United States" (Finding of Fact VIII).

"Under the facts and circumstances of this case, the termination of the subcontract on January 13, 1959, started the 90-day period running." (Finding of Fact VI)

"The 90-day period within which plaintiff was allowed under the Miller Act to give written notice to defendant Kelley, the general contractor, of its claim expired on April 11, 1959. Plaintiff was not reasonably diligent in making its claim." (Finding of Fact VII)

The District Court heard two full days of testimony on April 30 and May 1, 1963. At the conclusion of the second day, appellant rested and appellees moved to dismiss the action. The District Court took the matter under advisement and adjourned the trial until 10 a.m. the following day, at which time the court orally delivered a prepared opinion. Because this court has indicated it will consider a memorandum opinion to provide a more ample understanding of the legal issues and to interpret or supplement the findings (see *American Pipe and Steel Corp.* v. *Firestone Tire & Rubber Co.* (CA 9, 1961) 292 F.2d 640, 642) we are reprinting the court's opinion as Appendix A to this brief.

QUESTIONS PRESENTED

Appellant misstates the question on appeal as "whether a supplier has the full statutory period of ninety days in which to give the required notice." (App. Br. p. 5). The question which this court remanded to the District Court was whether as a factual matter in

this case the "termination of the subcontract should have started this period running." On this issue, the District Court found, after hearing appellant's case, that, under facts and circumstances, it did. (See Findings VI, VII and VIII, supra, pp. 3-4.)

Appellant did not make the transcript of testimony or the evidence a part of the record on appeal herein. These findings cannot be attacked therefore as unsupported by the record. This court should not be asked to speculate as to what labor and materials or equipment rentals are the subject of appellant's remaining claim and ignore the above findings of the court.

See McBee v. U. S. (C.A. 10, 1942) 126 F.2d 238; cert. den. (1942) 317 U.S. 691, 87 L. ed 554, 63 Sup. Ct. 263.
Leimer v. Mut. Life. Assur. Co. (C.C.A. 8, 1939) 107 F.2d 1003.
Hargraves v. Bowden (C.A. 9, 1954) 217 F.2d 839.

ARGUMENT

I. The giving of the 90-day notice is a condition precedent meant to protect a general contractor from double liability and to require diligence on the part of a supplier having no contractual relation with the general contractor.

The 90-day notice required by the Miller Act is a condition precedent to recovery, of which the burden of proving is on the claimant.

Fleisher E. & C. Co. v. United States (1940) 311 U.S. 15, 61 S. Ct. 81, 85 L. ed. 12.

Bowden v. United States (C.A. 9, 1956) 239 F.2d 572; cert. den. sum. nom. United States ex rel Mallory v. Bowden (1957) 353 U.S. 957, 77 S. Ct. 864, 1 L. ed. 2d 909.

Cooley v. Barten & Wood, Inc. (C.A. 1, 1957) 249 F.2d 912.

United States v. Mass Bonding & Ins. Co. (C.A. 3, 1959) 272 F.2d 73.

The legislative history cited by this court in the *Bowden* case indicates clearly the equitable requirement of diligence on the part of the supplier.

> " 'One protected by the bond must be vigilant in the prosecution of his rights thereunder or take the chance of finding the bond depleted by the executions of those more prompt than he, or perhaps find the door entirely closed against his suit by limitation. "Equity aids the Vigilant" ' H. Rep. No. 1263 (74th Cong., 1st Sess.)." (239 F.2d at p. 578)

The court's finding in this case was that "Plaintiff was not reasonably diligent in making its claim." (Finding of Fact VII).

II. On rented equipment, the notice period runs from the time the equipment was last available for use in prosecution of the work (i.e., was last located at the job site).

Plaintiff's brief, at page 7, states that "Under the Act appellant had ninety days after whatever date the law establishes as the date upon which the ninety day period commences." This date is specified in the statute as "the date on which such person did or performed the last of the labor or furnished or supplied the last of the material * * *." (40 U.S.C.A., Section 270b)

With respect to labor or items of material actually furnished, the date, of course, is determined by the date of delivery. With rented equipment, however, "the notice period runs from the time the equipment was last available for use on the project."

United States v. Campbell (CA 9, 1961) 293 F.2d 816; cert. den. (1962) 368 U.S. 987, 82 S. Ct. 601, 7 L. ed. 2d 524.

That appeal involved two suits under the Miller Act tried together but decided separately. In March, 1956, plaintiff leased earth moving equipment to a subcontractor on each of two public projects, one at Fort Funston and the other at Travis Air Force Base. Campbell was the prime contractor on both projects, but the sureties were different on each job—Fidelity on the Funston job and Phoenix on the Travis job. Plaintiff's original lease agreement was for the subcontractor to use the equipment at Funston and not elsewhere, but subsequently plaintiff agreed to the use of the equipment at Travis. The District Court awarded plaintiff judgment against Fidelity on the Funston job for rental for the period during which plaintiff's equipment was "located" or "available" at the Funston job site, less an amount of rental previously paid plaintiff by the subcontractor. In appealing this judgment, plaintiff argued that the award was inadequate

> "* * * because it was based upon the *actual use* of the equipment at the *Funston* project; appellant should be compensated, it contends, for the time during which the equipment was *available* for use at Funston, even if it was not actually used all the time. This, however, is a false issue (and the battle of case authority which the parties have en-

> gaged in with respect to it is irrelevant), for the court's computations purport to award rent for the time during which the equipment was 'located at' Funston * * * and it does no appear that 'available at' means anything other than 'located at,' especially when it is noted (as will be shown below) that appellant's computation of the 'availability' of particular equipment at various places corresponds significantly and almost precisely with the court's computation of when the equipment was 'located at' those places." (293 F. 2d at p. 818)

Thus, the court in the Fidelity case concerning the Funston job held that leased equipment is "supplied in connection with the bonded job" within the meaning of the Miller Act only while it is "available for use" or "located at" the job site. In fact, the claimant in that case admitted, and the court agreed, that to argue for more than such result would be "inequitable." The court went further and indicated that recovery of more than such amount would be "beyond the contemplation of the Act."

> "Appellant does not contend, however, that the surety on the Funston project should be held for the whole amount of rental allegedly due for equipment used on both projects. It admits that such a result would be inequitable. Furthermore such a result would be beyond the contemplation of the Act. 40 U.S.C.A. § 270b makes the surety liable only for material supplied in connection with the bonded project." (293 F. 2d at p. 818)

The second Campbell case relating to the claim against Phoenix on the Travis job dealt with the question of when rental or leased equipment is "last furnished" for purposes of determining timeliness of the required 90-day notice. The District Court had denied

claimant recovery and this court affirmed that judgment. In so doing, the court reaffirmed *Bowden* that the required notice is a condition precedent to a claim against the bond. Appellee Phoenix had argued that the leased equipment was last furnished to the Travis job the date it was first delivered to the subcontractor, arguing for an analogy to the delivery of materials. The court would not accept that argument.

> "With respect to materials the crucial date to start the notice period is, of course, the date the materials are delivered. So, by analogy appellee arrives at the conclusion that the crucial date for equipment is the date the equipment is delivered.
>
> "The lack of merit in appellee's position seems obvious. Delivery of the materials completes the seller's obligation, and full payment becomes due either at once or at a specified time thereafter. Delivery of equipment under a lease, on the other hand, is only the beginning of lessor's obligation. *He must allow the equipment to remain in the hands of the lessee for such time as is specified by the lease arrangement. Payment is not due at once, but at various times during the lease period, usually on a periodic basis. Under appellee's theory, a lessor would, more frequently than not, have to file a Miller Act notice even though the lessee is not in default.* If the lease was to run for more than three months, the lessor, in order to protect the rights would have to file a notice after three months, *even though the lessee had met every rental payment promptly.*
>
> "We hold the correct solution of the problem is the one advanced by appellant. It contends the notice period runs from the time the equipment was last available for use on the project. In the instant case, the parties agreed by stipulation that December 5, 1956, was the last day on which any of the

> leased equipment was at the Travis job site. Thus the one notice which the court found to be adequate from a contract standpoint was not timely. This is plaintiff's Exhibit No. 5, a letter dated *March* 8, 1957, and mailed to the contractor (Campbell) on March 12, 1957." (293 F. 2d at p. 820) (Emphasis added)

The only case other than *Campbell* which we can find dealing with the question of when rental equipment is last furnished is the case of *United States for use of Marlin* v. *F. D. Rich Co.* (ND Fla., 1961) 199 F. Supp. 939; Aff'd. per curiam sub. nom. *F. D. Rich Co* v. *United States* (C.A. 5, 1962) 308 F.2d 807. In that case plaintiff rented certain construction equipment to a subcontractor on August 30, 1960, for an initial one-month rental period. The subcontractor defaulted on the job and the payment of the rental and the equipment lay idle *on the job site* from September 30, 1960, until April 20, 1961, when it was repossessed by plaintiff. Thereafter and within 90 days of April 20, 1961, plaintiff gave the general contractor the required 90-day notice. The question presented was whether the September 30 or the April 20 date was the date upon which the equipment was last furnished. The court dismissed the action holding that the September 30 date was controlling.

> "Had plaintiff been diligent, he could have apprised Rich or the sureties within the 90-day period, and could have protected his rights under the Miller Act. Plaintiff knew where his equipment was, and did in fact retrieve it after a delay of almost seven months. While the Miller Act was designed for the purpose of protecting laborers and materialmen to the extent of their labors and materials fur-

> nished, the Act places upon these preferred persons an obligation of certain diligence" (191 F. Supp. at p. 941)

As previously indicated, the District Court in the case at bar found that plaintiff was not reasonably diligent. The undisputed evidence before the District Court which had previously been before this court indicated that plaintiff contracted with defendants Ramage and Ayala to receive substantial payments every two weeks commencing November 27, 1958. Despite all the claims made by plaintiff, no payment was ever received from a subcontractor other than a "bum check." Plaintiff's president admitted that he went to the job site at least two times in December, 1958, to check the job and was made aware of all the problems that the subcontractors were having in attempting to prosecute the work with the defective tractors. The District Court in his oral opinion noted that "there was trouble with the collection of this account from the end of the first month. We note that no payment was made thereon except a NSF check * * *." The District Court disbelieved testimony of plaintiff's officers that they were not concerned about the default and concluded "obviously it appears to me that they were and should have been."

The *Campbell* and *Rich Co.* cases expressly indicated the significance of the lease period and the question of the lessee's defaults in payment as they relate to the diligence of the supplier.

III. Under the facts and circumstances of this case, appellant was not reasonably excused from performance of the statutory conditions precedent.

The District Court in its decision held that the date of January 13, 1959, when the equipment was removed from the site, under the *Campbell* case, "must govern as to the running of the statute * * * unless we find that the claimant was reasonably excused from performance and therefore the circumstances of each case must govern." The court following the instructions of this court on the remand determined that the January 13, 1959, date was controlling under the facts and circumstances which were before him, the record of which appellant did not choose to bring before this court. The District Court further found that the facts and circumstances did not justify extending the statutory 90-day period to accommodate a non-diligent claimant.

The only case cited by appellant is not in point. *United States* v. *Endebrock-White Co.* (C.A. 4, 1960) 275 F.2d 57, 79 ALR2d 836, dealt with a supplier furnishing materials to a subcontractor where the purchase orders specifically indicated that the materials were intended for a bonded job. The court held that wrongful diversion by an employee of the last item ordered by a party who was at the time a bona fide and existing subcontractor, would not cause the 90-day period to run from the next to last item furnished. Compare: *United States* v. *Peter Reiss Construction Co.* (C.A. 2, 1959) 273 F.2d 880, 78 ALR2d 409; affirming (ED NY, 1959) 174 F. Supp. 264.

In the case at bar, defendants Ramage and Ayala after January 13, 1959, were not subcontractors on a bonded job. In *Endebrock-White,* Mechanical was in fact the subcontractor when the last item was ordered and furnished on December 31, the date when the 90-day period commenced. Further, the District Court here specifically found that after January 13, 1959, plaintiff did not furnish any labor or materials used in the prosecution of the work on the bonded job. See: *St. Paul-Mercury Indemnity Company* v. *United States* (C.A. 10, 1956) 238 F.2d 917.

CONCLUSION

Appellant asks this court to establish a rule that a *nondiligent* claimant may extend the time for commencement of the 90-day notice period by closing its eyes to the actual and objectively ascertainable facts. The District Court, on remand, determined that, under the facts and circumstances of this case, appellant was not diligent, and that it failed in its burden of showing why it should be excused from being governed by these objective facts.

Appellees pray that the judgment of the District Court be affirmed.

Respectfully submittted,

KOBIN & MEYER,
MCNEALY & MERDES,
By PAUL R. MEYER,
Attorneys for Appellees.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing brief is in full compliance with those rules.

PAUL R. MEYER

APPENDIX "A"

Opinion of the Court

At 10:00 a. m. on May 2, 1963, at Fairbanks, Alaska, The Court announced its decision on the defendants' motion to dismiss the foregoing action, as follows:

THE COURT: In arriving at a decision on the very important question raised by the defendants' motion to dismiss, by reason of failure of the plaintiff here to give the ninety day notice required by law, we must bear in mind first, the express provisions of the statute which gives a remedy, directs a remedy, and that is Section 270 (b) of Title 40, United States Code, which specifically requires as a condition precedent to the right of action—that is, it has been so held in many cases—that where a contractual relationship is with a sub-contractor and not the contractor, the supplier must give written notice to the contractor within 90 days from the date on which the last services were performed or material furnished, stating with substantial accuracy the amount of the claim, the nature of it, which may be served by registered mail.

The reason for this rule has been discussed many times by the Courts. It is intended by Congress for the protection of the contractor, in order that he may possibly take care of the claim before paying off the sub-contractor, and also for the protection of the bonding company, in order that the company may meanwhile prevent default or loss, as is often done. It is also for the protection of the supplier, so that he has a claim against the contractor and the bonding company, providing he is diligent in giving such notice.

It is a matter which we cannot waive because it is a condition precedent to suit, and is therefore not merely technical.

We must also bear in mind that the claim must be for labor and materials furnished in the prosecution of the work, and that the ninety day period begins to run from the date that the materialman did or performed the last of the labor or furnished the last of the material for which the claim is made.

It has been held many times that the statute applies to equipment rentals, but that such are likewise limited to rentals of equipment used in the prosecution of the work. And it has been specifically stated by the Court of Appeals for the Ninth Circuit in the case of United States vs. Campbell, 293 F. 2d 816, the period commences to run when the equipment was last available for use on the project. And that decision, of course, is absolutely binding upon this court.

So we have here then, the question, the fundamental question of when does the notice period commence in this case? In this connection I find a difference, a very material difference between the equipment supplier to claim against the lessee for rentals which, as Mr. Miller correctly stated, is ordinarily, according to their practice, a period running until the equipment is returned to their yard. That is quite reasonable, but does that apply to a claim against a contractor and his bond under the Miller Act?

I find that it does not. Doubtless plaintiff here would have just remedy against Ramage and Ayala, they could recover rentals until the equipment is returned. But that is not our problem here.

The problem here is whether Mr. Kelley, the contractor, and his surety, are responsible for such rentals. The answer is no. They can be responsible only for the use of the equipment when last available for use on the project or used in the prosecution of the work.

The sub-contractor was terminated on January

13, 1959, and the equipment removed from the site either then or very shortly thereafter. This date, then, must govern as to the running of the statute rather than the date, as contended by plaintiff, as to when plaintiff was informed of that fact, unless we find that the claimant was reasonably excused from performance, and therefor the circumstances of each case must govern.

Now I hold that the written notice of April 28, 1959, sent by registered mail to the defendant Kelley at the address at which he was then living and had his place of business, was sufficient notice under the Act, if timely made. I feel that counsel for plaintiff was very diligent in taking the action, as he has testified, best calculated to give notice, and that there is no reason why such notice is not in full compliance with the Act and, therefore, that the notice served by the marshal on May 12 is superfluous, and we are not particularly concerned with that date.

I have examined briefly the case cited to me by counsel of Houston Fire & Casualty Insurance Co. vs. United States, 217 F. 2d 727 (729), to the effect that oral notice to the contractor may be sufficient where written acknowledgement is made by the contractor of the claim. But we do not have that situation here, according to the evidence.

Now the Circuit Court has indicated that notwithstanding the failure of the contractor to give notice of the termination of the contract, the court may consider whether or not the plaintiff as a reasonably prudent supplier, should have known of it, or should have known of the removal of the equipment and the no longer use on the project of the equipment.

I am compelled to find from the evidence in this matter, that the plaintiff or supplier here, as a reasonably prudent person or supplier, should

have known that the equipment was no longer being used. Now we note that there was trouble with the collection of this account from the end of the first month. We note that no payment was made thereon except an n. s. f. check, of which Mr. Bentley was fully aware when the check was returned, on February 26th or thereabouts. We note that one of plaintiffs' mechanics was called to the site on January 30, at which time, according to the witness Phillips, the equipment was not on the site at all.

MR. COLE: Excuse me. Mr. Phillips testimony is not now before the Court Your Honor.

THE COURT: Well perhaps not, if we are strictly limited to the testimony of the plaintiff. I will reject that, strike that.

But that actually there is no dispute of fact that the sub-contract was terminated on January 13, and the Circuit Court has expressly so found in its opinion. The evidence does show that on February 16, the plaintiff was served with a summons and complaint in an action brought against them by Ramage and Ayala, and they made a counter claim in that suit as to their claim for rentals and so on, which was submitted to counsel, but that no claim was asserted against the contractor and his bond until April, although Mr. Bentley knew of his right to go after the contractor and the bond. He testified that he believed the equipment was not on the job at least at that time.

We note that counsel wrote to United Pacific Insurance Co., a defendant here, on February 24, stating that the account was past due and inquiring regarding the bond, but no notice was given the bonding company of this claim. We find that Mr. Miller was made aware of the trouble here, that his job was going bad, by a telephone call while he was on vacation, and on his return about February 4. He had heard rumors in February, I think,

and before, of trouble there. Both managed to seem willing to deny that they were greatly concerned about this default, but obviously it appears to me that they were, and should have been.

I also find that Mr. Kelley gave them notice of the equipment being removed on February 15, and not on March 20 as is claimed, or about which date the equipment was repossessed by plaintiffs.

I am therefore obliged to find that the plaintiff had ample time after the termination of the subcontract to make a claim against the contractor and surety within the ninety day period provided by law, that is, on or before April 11, 1959, and that they were not reasonably prudent in enforcing that right, and that the notice of April 28 was therefore not timely made.

Now this does not mean, as urged by counsel, if we enforce this rule it will be impossible to collect rental accounts against a contractor and surety. What is required is reasonable diligence on the part of the supplier and a showing that in good faith a supplier believed, and had a right to believe, that the equipment was still being used on the job. And I cannot find that that is so, except to, possibly, February 15. But after that plaintiff had nearly two months in which to assert their remedy against the contractor and surety.

I realize that plaintiffs made a bad deal here and have suffered loss, and if we were governed by sympathy, I sympathize with their loss. But we are not, of course, and I feel that Mr. Kelley is not responsible for their loss, of course, but some irresponsible people who mislead the plaintiffs into taking this equipment. A greater part of their loss, of course, has already been disposed of in that they unfortunately made a conditional sale, on these tractors. The other loss is not great, relating to the other equipment rentals, and there is a greater ques-

tion as to labor, as to whether such was supplied under their contract for use of the tractors and/or repair of the tractors.

And I am therefore compelled to grant the motion of the defendants for dismissal upon the grounds that the condition precedent to commencing the action was not complied with. The plaintiffs' complaint may therefore be dismissed with costs. Under the Miller Act it is held that we can allow attorney fees in the discretion of the Court, according to State law, which again is in the discretion of the court. We have no schedule for it. I feel in view of the good faith of plaintiffs in asserting this claim and in view of their loss, that would be unjust, to assess attorney fees. Therefore I will not assess such fees, but only costs.

I do not recall what, if anything was done with reference to the complaint against Ramage and Ayala who were made parties to the suit. I presume that if counsel was interested in judgment against them, we could do so.

MR. COLE: Yes, Your Honor. I shall submit such a judgment.

THE COURT: By default, because they have never appeared. I don't know how much good it will do.

MR. COLE: Yes, Your Honor, we would like that judgment. May I make one further inquiry about the court's findings? As I understand the Court's opinion, the Court has adopted Feb. 15 as the date upon which we should have known the equipment was no longer on the job?

THE COURT: Yes, but I cannot find that that is the date from which the notice commences to run.

MR. COLE: I understand.

THE COURT: I am considering that date with reference to the reasonable diligence in giving notice.

MR. COLE: But at any rate that's the date the Court finds we should have known the equipment was no longer on the job, after that date?

THE COURT: Correct.

MR. COLE: Fine. Thank you.

THE COURT: At least after that date. With regard to your judgment against Ramage and Ayala, of course the equipment was repossessed and I presume you elected your remedy there so far as the tractors were concerned?

MR. COLE: Well, I can discuss that with the Court.

THE COURT: But as to the other relief demanded, I think surely you are entitled to a judgment.

MR. MERDES: Your Honor, Mr. Meyer moved for dismissal of the action.

THE COURT: Yes. Excuse me. The action will be dismissed as the defendants James H. Kelley and the United Pacific Insurance Co. I am glad to make that correction. The Ninth Circuit reminded me that the dismissal of a complaint is not the dismissal of an action. Very well.

MR. MERDES: Thank you, Your Honor. Would the Court's remarks stand as the findings?

THE COURT: No, not an oral decision.

MR. MERDES: I see.

THE COURT: I am just thinking of that. I would request that counsel for plaintiff prepare appropriate findings of fact, conclusions of law and judgment. There is now pending a rule becoming effective July 1, that the Courts must draw their own judgments, so we cannot ask the attorneys to do it, but that rule is not yet effective, and besides which it does not say we cannot ask the atttorney to draw findings of fact, as near as I can figure.

MR. MEYER: Did your Honor mean counsel for the defendant?

THE COURT: Yes—counsel for the defendant. I'm sorry. Is there anything further? If not, I

believe that concludes my work in Fairbanks so we will adjourn this session sine die.

MR. MEYER: I wonder if I could ask a question about Your Honor's findings with respect to preparing them. Has Your Honor made any finding with respect to whether plaintiffs had been advised prior to Mr. Miller's leaving on his vacation of the probability of the termination of this subcontract?

THE COURT: Well, not expressly. I think that is true—well, no, I wouldn't go that far. I don't think it is necessary. We will just fix this date of February 15 as the date on which they were fully informed that the equipment was no longer on the job.

MR. MEYER: You don't mean by that finding to make an implication that they weren't informed before that, or didn't have reason to believe before that?

THE COURT: Well I concur that you may also include a finding that they had reason to believe before that.

MR. COLE: Your Honor, I would like to have a finding as to the date on which, as a reasonable supplier, we were on notice. Now as I understand the Court's opinion, the Court said February 15 was the date on which the Court finds that we were on notice, as of that date, and I accept that date as the date on which the Court so finds.

THE COURT: Well, counsel's request was whether they could put in a finding whether they had reason to believe the equipment was removed prior to that time. I don't think I will go that far. I think doubtless they had reason to believe there was trouble, plenty of trouble, but I can't find they had reason to believe the equipment was removed prior to that time. I don't believe it's necessary.

MR. MEYER: You are not finding to the contrary? That's the only thing — I mean you are not finding negatively on that issue? adversely to

our suggestion? You simply don't feel it is necessary to make a finding on that, and you are not?

THE COURT: I don't feel that it has been sufficiently shown, and also that it is not necessary.

Pardon me, there is one thing more. I will, of course, be back in Anchorage next Monday or Tuesday, so the findings and judgment may be submitted to me there.

(Court was then adjourned)

No. 18826

In the

United States Court of Appeals

For the Ninth Circuit

CHARLES ALBERT GARRETT and DOROTHY ELIZABETH DARLING,

Appellants,

vs.

THE UNITED STATES OF AMERICA,

Appellee.

APPELLANT'S BRIEF

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I N D E X

TABLE OF CASES CITED

OTHER AUTHORITIES CITED

NO. 18,826

IN THE

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

CHARLES ALBERT GARRETT and
DOROTHY ELIZABETH DARLING,

Appellants,

vs.

THE UNITED STATES OF AMERICA,

Appellee.

A. STATEMENT OF THE CASE

On or about March 28, 1963, the Grand Jury in the District of Arizona returned a one count indictment against each of the Appellants herein charging the receiving, concealing and facilitation of the transportation and concealment of approximately 37 grams of heroin, a narcotic drug after the importation thereof into the United States in violation of Title 21, United States Code 174. On or about April 8, 1963, each Appellant entered a plea of not guilty to the aforesaid indictment. Thereafter on

June 11, 1963, trial was had to a jury and on that same day, after only 20 minutes deliberation, verdicts were returned finding each appellant guilty as charged. Motions for Judgment of acquital on behalf of each of the said Appellants were denied at the close of the prosecutions case and at the close of all the evidence. Appellants filed Motions for New Trials on June 13, 1963 and the same were heard and denied on June 24, 1963. Thereafter, on June 24, 1963 the Court entered Judgment on the verdict of the Jury and committed the Appellant, Garrett to the custody of the Attorney General or his authorized representative for imprisonment for a period of 8 years; the Court committed Appellant Darling to the custody of the Attorney General or his authorized agent for imprisonment for a period of 5 years, and recommended that she be hospitalized for Narcotic addiction. Subsequent thereto on June 26, 1963, Appellants filed their respective Notices of Appeal from the verdicts and judgments.

This appeal is prosecuted to vacate and set aside the judgments of guilty and the terms of imprisonment imposed pursuant to the Court's judgments and commitments.

B. EVIDENCE

The following is a summary of the Evidence:

1. Testimony of M. R. Rogers.

M. R. Rogers testified that he was a U.S. Customs Agent and that on November 3, 1963, he was riding with Customs Agent L. O. Viles in a patrol car. That on the aforesaid date he observed a Colored Male along the boundary fence that separates the United States from the Republic of Mexico. He further testified that he did not recognize the individual he referred to in his testimony. He further testified that upon observing the aforesaid, he returned to his headquarters and secured another vehicle and returned to the area. That about 1:00 p.m. he observed a Lincoln convertible pass the area. That he informed Agent Viles as the automobile passed from his view. That later he arrived at an intersection and found Agent Viles, a police officer named Salamon, and the two Appellants at an intersection. That he assisted in a preliminary search which produced nothing and later that Appellant Darling removed a package from under the skirt in the office of the Agency and advised them that Appellant knew nothing whatsoever about the package or its' contents. (R. 16-46)

2. Testimony of Randolph R. Aros.

Randolph R. Aros testified that he was a Customs Agent and that on the 3rd of November, 1963 he was near the International fence after being summoned by Agent Viles. That he observed a man who he identified as the Appellant Garrett near the fence and make a throwing motion and that an object

went over the fence. That later a car drove up and Appellant Darling alighted therefrom. That the automobile containing both Appellants was later stopped and Appellants taken to the Agency office. That Mr. Garrett denied any knowledge of the existence of the package, and Appellant Darling confirmed this statement. That he discovered no contraband as a result of a search of Appellant Garrett's person and the automobile. That Appellant Garrett advised him that he had taken Appellant Darling to the dentist on the Mexican side and produced a receipt as evidence thereof, and that he himself had also visited a dentist office. (R. 46-95)

3. Testimony of David Salamon.

David Salamon testified that he was employed as a police officer by the City of Nogales, Arizona. That he assisted in stopping an automobile containing Appellants at the request of Agent Viles. (R. 96-101)

4. Testimony of Leonard Viles.

Leonard Viles testified that he is a Customs agent and that on November 3, 1963, he saw a colored man walking along the International fence. That he later saw Appellants cross into the United States at the Grand Avenue gate. That he later stopped the automobile containing Appellants and searched and found nothing. That

Appellant Garrett denied any knowledge of any contraband, and Appellant Darling later produced a package and confirmed that Appellant Garrett had no knowledge concerning the same. He also testified that Appellant Garrett produced a dental appointment slip and advised him that Appellant Darling had also visited another Dentist in Mexico. (R. 101-116)

5. Testimony of Jack B. Smith.

Jack B. Smith testified that he was a Customs Inspector and custodian of seized merchandise. That he received Governments Exhibits 1 C and 1 D on the 5th of November 1962 and he initialed the same and mailed them to the Chief United States Chemist. He further testified that he had received the exhibits from Agent Leonard O. Viles and he also identified Government's Exhibit 1 D as the box he used to mail said exhibits and that he did not see Government's Exhibits 1 through 1 D until he observed them in a vault in the Customs Inspection Station the day before the trial. That he turned the same over to Mr. Lindberg. (R. 116-123)

6. Testimony of George S. Hill.

George S. Hill testified that he lived in Whittier, California and that he is a chemist for the United States Customs laboratory. That Government's Exhibit 1 A was

discovered by him in the laboratory in a sealed condition. That he examined the contents thereof and discovered that the same contained heroin and sent the same back to Nogales, Arizona. He later stated on cross examination that the Chief chemist mailed the same back to Arizona, and that he had no knowledge as to whether the package had been opened and resealed. (R. 123-130)

7. Testimony of Jack Sheaffer.

Jack Sheaffer testified that he was a professional photographer and employed by the Arizona Daily Star Newspaper. That he was in the company of counsel for Appellants (Benjamin Lazarow) and Agent Aros at the foot of the hill near where the objects were allegedly thrown. That Agent Aros at that time stated that there was too much brush to observe the landing of the object and that he did not see Appellant Garrett throw the object. He also testified that he took the pictures of the area which were received in evidence as Defendant's exhibits. (R. 135-142)

8. Testimony of Charles A. Garrett.

Charles A. Garrett testified that he agreed to take Appellant Dorothy Darling to Nogales, Sonora, Mexico on November 3, 1963 and secured one L. T. Hill to drive them over from the City of Tucson. That Mr. Hill parked the automobile on the American side

of the border. That Appellant Darling went to the dentist in Mexico and he went in search of another dentist. That upon returning to the area where the car was parked, Mr. Hill was missing and they drove around in an effort to locate him. That they were stopped by the Customs agents and searched. That he advised the Agents that he had no contraband and had merely gone to the dentist and so had Appellant Darling. That he was at one time lost on the Mexican side due to his unfamiliarity with the Mexican side of the border. (R. 142-191)

C. ARGUMENT

The Court erred in failing to grant Appellant Garrett's Motion for Judgment of Acquital at the close of the Government's case and at the close of all the evidence in view of the fact that said evidence was grossly insufficient on both occasions to sustain a conviction on the count contained in the indictment. (R. 132-134) The entire record fails to actually disclose anything other than the fact that Appellant was in close proximity to contraband of which he had no knowledge. This fact is properly indicated by the testimony of the disinterested witness Jack Shaffer. (R. 135-141), also by virtue of the fact that Agent Aros could not specifically testify that Appellant Garrett made anything more than a throwing motion. (R. 46-52).

The evidence further indicates that Appellant Darling virogously and continually insisted that Appellant Garrett had nothing to do with, and knew nothing about any contraband found in her possession. (R. 45), (R. 77), and (R. 109-110). According to the testimony of the Customs Agents the package was secured from Appellant Darling from a concealed area under her skirt and was delivered to them outside the presence of Appellant Garrett. (R. 45-46), (R. 57) and R. 116).

In Glover vs. United States, 306 F. 2nd 594, the Court held:

> "While the evidence may have been sufficient to cast suspicion upon Glover, that was not enough. Evidence which creates mere suspicion of guilt is not enough. Guilt may not be inferred from mere association."

also citing Thomas vs. United States, 239 F. 2nd 7, Corbin vs. United States, 253 F. 2nd 649, Erwing vs. United States, 296 F. 2nd 320, and Mills vs. United States, 293 F. 2nd 609.

Further, the Court erred in allowing hearsay evidence into the proceeding and also by failing to advise the jury to disregard the same when it was called to his attention. That the aforesaid evidence was grossly improper and highly prejudicial

against both Appellants and precluded a fair and unadulterated consideration of their cases by the jury. (R. 20-21, 23-24, 47-48, 55, 103 and 107). The rule has long been much akin to the one cited in United States vs. Campanaro 63 F. Supp. 811, wherein the Court said:

> "Evidence which does not derive its value solely from the credibility of witness, but rests also on veracity of another person is 'hearsay' and is ordinarily inadmissible."

The transcript indicates serious error particularly as the same would concern Appellant Darling wherein the Court allows the testimony of Agent M. R. Rogers to stand as concerns his purported "expert" testimony as to the nature of the alleged contraband as being heroin when in fact no foundation was laid for such testimony. (R. 27). Concerning this the Court held in Lyles vs. United States, 254, F. 2nd 725:

> "A fact can be testified to by any witness, but with few exceptions, opinions can be given in evidence only by an expert and reasons for his opinions are part of premise for allowing expert to testify."

It thus becomes apparent that the language in U. S. vs. Markowitz, 176 F. Supp. 681, becomes very material in the case at bar when the Court advised:

"Unless there is substantial evidence of facts which exclude every other hypothesis but that of guilt, it is the trial Judge's duty to instruct jury to return verdict for accused, and where all substantial evidence is as consistent with innocence as with guilt, it is duty of Appellate Court to reverse a judgment against accused."

D. CONCLUSION

For the reasons hereinabove set forth and argued, I am satisfied that this Honorable Court, upon examination of the record, will be convinced that these Appellants are entitled to have this matter reversed, the indictment quashed and the case dismissed, and accordingly, I pray that the judgments of guilty and the accompanying penalties imposed be set aside and held for naught and that this Honorable Court enter appropriate orders to that end.

Respectfully submitted,

ROBERT C. RHONE, JR., Esq.

2130 Downing Street
Suite 203
Denver 5, Colorado-80205

December, 1963 Attorney for Appellants

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

ROBERT C. RHONE, JR.

No. 18826

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

CHARLES ALBERT GARRETT and
DOROTHY ELIZABETH DARLING,
Appellants,

vs.

UNITED STATES OF AMERICA,
Appellee.

Upon Appeal from the United States District Court
for the District of Arizona

BRIEF FOR APPELLEE

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No. 18826

IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

CHARLES ALBERT GARRETT and
DOROTHY ELIZABETH DARLING,
Appellants,

vs.

UNITED STATES OF AMERICA,
Appellee.

UPON APPEAL FROM THE
UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

BRIEF OF APPELLEE

JURISDICTIONAL FACTS

Appellants, having been indicted on March 26, 1963, by the Grand Jury for the District of Arizona, entered, respectively, pleas of not guilty to the Indictment on April 8, 1963. A verdict of guilty was returned by the jury on June 11, 1963 as to each defendant and they were adjudged guilty by the Court on June 24, 1963, immediately after the denial by the Court of Motions for New Trial filed by each appellant.

This Court has jurisdiction under Title 28 United States Code, Section 1291.

STATEMENT OF FACTS

Customs Agents Viles and Rogers, during a routine patrol, observed a colored male in the vicinity of the International fence between the United States of America and the United States of Mexico who aroused their suspicions (Transcript of Record, Volume Two, hereinafter designated TRT, P 16-20, 102-103). As a result thereof, another Customs Agent, Aros, was called and, after obtaining a portable radio and binoculars, he situated himself on a little hill overlooking the area where the man had been seen and maintained a lookout. (TRT P 47-48). Thereafter, Mr. Aros observed a man, whom he identified as the Defendant Garrett, get out of a Mexican Yellow Cab on the Mexican side of the border, look to both sides, and make a throwing movement. Mr. Aros observed a black object come over the International fence toward him. (TRT P 50, 51, 67). Agent Aros described the man and his actions to the other agents by radio (TRT P 51). After Mr. Garrett walked away from the area, Aros found the object(the location of which he had fixed by reference to cars on the Mexican side of the border), opened it, observed its contents to be a grayish-brown powder which he assumed to be heroin, placed an initialed slip of paper therein, resealed and left it where he had found it. (TRT P 52).

Mr. Garrett was next observed by Agent Viles (recognized by the description furnished by Mr. Aros) in the company of Miss Darling entering the United States from Mexico. He identified both as the defendants in the case. (TRT P 104-105). A Nogales, Arizona, police officer followed the appellants at the request of Viles and observed them get into a 1956 Lincoln convertible in Nogales, Arizona, and drive off in a southerly direction. (TRT P 96). The appellants were thereafter under virtually continuous surveillance by Officer Salmon (TRT P 97), Agent Viles (TRT P 106) and Agent

Rogers (TRT P 23), and they proceeded, with Mr. Garrett driving, to precisely the spot where Mr. Aros had found the package (TRT P 53). The car stopped briefly and, after it departed the area, Mr. Aros, who saw the car door open and heard it slam, sought the package, but could not find it. (TRT P 53-54).

Thereafter, having received this information, the other officers followed and stopped the automobile (TRT P 108) and ultimately recovered the package from Miss Darling. (TRT P 24-26, 56-57, 106-110). The package and contents, after having been duly identified, were admitted into evidence (TRT P 131). The contents, having been previously analyzed, were designated to contain heroin (TRT P 127).

Mr. Garrett crossed from the United States into Mexico with Miss Darling and went with her directly to a dentist's office, according to his testimony (TRT P 146-147), where he left her. (TRT P 173). He then testified to leaving the building and office while Miss Darling was undergoing treatment and that when he returned she was *just coming out* of the dentist's office—about twenty minutes later. (TRT P 146-149, 173-175).

At the conclusion of all the evidence and following the Court's instructions, the jury returned the aforesaid verdicts of guilty as to each defendant.

OPPOSITION TO SPECIFICATIONS OF ERROR

Although Appellant's brief does not contain specifications of error, it appears from the Argument contained therein that Appellants rely on Items First, Second and Fourth as set forth in the Statement of Points in the Designation of Record on

Appeal as to each defendant (Transcript of Record, Volume I, P 29-32). As to those, Appellee replies as follows:

1. The record reflects that the conviction of each appellant is supported by substantial evidence.

2. No hearsay evidence was admitted over timely and proper objection and the Court was not requested to instruct the jury to disregard any evidence to which objection was sustained.

Appellants argue that certain expert opinion evidence was admitted without foundation, to which Appellee replies as follows:

3. The testimony designated as objectionable by Appellants was not substantive expert testimony and was not heretofore objected to, designated, or specified as error.

SUMMARY OF ARGUMENT

1. The verdict of guilty should be sustained in the absence of plain error unduly prejudicing the rights of the defendant in that, taking the view most favorable to the Government, there is substantial evidence to support it.

2. Testimony by a witness of his conversation at a prior time does not constitute hearsay, nor does the overheard conversation of another if related by the witness merely for the fact and not the truth thereof.

3. In the absence of timely and proper objections the Appellate Court will take cognizance of alleged error only if plain error prejudicial to the defendants.

ARGUMENT

1. SUBSTANTIAL EVIDENCE SUPPORTS THE VERDICT.

It is almost axiomatic, requiring no citation, that if, taking the view most favorable to the Government, a verdict of guilty is supported by substantial evidence it must be sustained. *Glasser v. United States,* (1941) 315 U.S. 60, 74 S.Ct. 457, 86 L.Ed. 680. *Substantial evidence,* although variously defined by the Courts, has been accepted by this Court as ". . . such relevant evidence as a reasonable mind might accept as adequate to support a conclusion . . ." *Woodard Laboratories v. United States,* (C.A. 9th, 1952) 198 F.2d 995, 998. The Court in *Woodard* acknowledged the proposition that it is not the function of the Appellate Court to weigh the evidence or to determine the credibility of witnesses.

Although not supported by all of the authorities cited by Appellants, the rule of law that a conviction may not be based on mere suspicion is settled and so stated by the trial court as part of the instructions given the jury (TRT P 192). The record, which Appellant contends fails to disclose anything as against Garrett except close proximity to contraband, reflects, as reviewed in the Statement of Facts, the eye-witness testimony of Aros demonstrating the closeness of that proximity. The description of the man making the "throwing motion" was sufficiently accurate for Mr. Viles, who had never seen the Defendant Garrett, to recognize him and initiate surveillance. Mr. Garrett's driving to and stopping at the precise spot where the narcotics fell in the United States is particularly persuasive when, by his own testimony, Miss Darling could not have known that location. Her actual possession and his actual, or at least constructive, possession under the appropriate instructions, as given by the Court, (TRT P 198-200)

give rise to the statutory presumption as to importation and knowledge. *Title 21 U.S.C.* § *174.*

Although the quotation on page 10 of Appellant's brief could not be found in the case cited, the nature thereof was such as to inspire a search for its source. In the case of *United States v. J & R Transport Company,* (D.C. E.D. Pa. 1959) 176 F.Supp. 871, 872, the quotation appears almost verbatim. In that case the Court went on to say that as an instruction that language had been criticized in *Holland v. United States,* (1954), 348 U.S. 121, 75 S.Ct. 127, 99 L.Ed. 150.

The evidence, as above, and it is submitted, as a whole, was sufficiently strong to banish all reasonable doubt as well as being "adequate to support a conclusion."

2. WITNESSES' OWN PRIOR CONVERSATION NOT HEARSAY NOR IS THE FACT OF ANOTHER'S CONVERSATION

3. ONLY PLAIN AND PREJUDICIAL ERROR RECOGNIZED ON APPEAL IN ABSENCE OF OBJECTION

(a) Appellant's set forth the conversation of Viles as related in the testimony of Rogers (TRT P 20-21) as hearsay. Objection thereto was over-ruled (TRT P 21).

(b) Appellants specify R. 23-24 as containing objectionable hearsay. Objection was made (TRT P 25) and sustained.

(c) Appellants specify R. 47-48 as objectionable. No objection thereon is recorded.

(d) Appellants specify R. 55 and R. 103 as containing objectionable hearsay. No hearsay objection is recorded thereon.

(e) Appellants specify R. 107 as objectionable. The objection asserted was over-ruled (TRT P 107).

No request was made of the Court that the jury be instructed to disregard the above testimony given. The failure thereof limits this Court's consideration thereof. *Myers v. United States,* (C.A. 3d, 1929), 36 F.2d 859.

As to Items (a) and (e), the Court properly over-ruled the objection asserted in that the conversations related by the witness were either his own statements of what he did or related for the fact of the conversation as precedent to action on his part. As stated by the Court in the case cited by Appellants:

> ". . . However, not every oral or written extrajudicial statement offered in evidence comes within the hearsay rule. It is only where the extrajudicial statement is offered to establish the truth of the fact so stated that the hearsay rule can apply. Where the extrajudicial statement is offered without reference to the truth of the matter extrajudicially asserted, but merely to prove that the oral statement, in fact, was made or that a written statement, in fact, exists, then evidence is without the hearsay rule. . . ."
>
> *United States v. Campanaro,* (D.C. E.D. Pa. 1945), 63 F.Supp. 811, 814.

As to Item (b), objection was sustained and the witnesses' testimony prior thereto falls into the above category.

As to Items (c) and (d), no objections having been raised the objections cannot be raised on review unless in light of all the facts so prejudiced Appellants as to deny them a fair trial. *Hill v. United States,* (C.A. 9th, 1958), 261 F.2d 483.

It is submitted that, even if objectionable, the testimony was insignificant in view of all the facts and not prejudicial.

To the same effect is Appellants' Argument as to purported "expert" testimony of M. R. Rogers (TRT P 27). No objection was raised thereon below and, as aforesaid. cannot now be raised in the absence of plain error. *Hill v. United States, supra.* Further, it is apparent that Rogers was merely testifying to what he did and said and not as giving substantive expert testimony. Further, expert opinion having been subsequently received as to the contents of the package recovered (TRT P 127), Rogers' testimony could not have been projudicial to Appellants.

CONCLUSION

The rulings of the Court having been proper, no error of consequence having been shown and the jury's verdict having been supported by substantial evidence, it is submitted, the judgment should be affirmed.

Respectfully submitted,
C. A. MUECKE,
United States Attorney
For the District of Arizona
JOHN E. LINDBERG
Assistant United States Attorney
Attorneys for Appellee

I certify that, in connection with the preparation of this Brief, I have examined Rules 18 and 19 of the United States Court fo Appeals for the Ninth Circuit, and that, in my opinion, the foregoing Brief is in full compliance with those rules.

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Three copies of within Brief of Appellee mailed this 24th day of January, 1964, to:

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No. 18828

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

WILLIAM BRUCKER,

Appellant,

v.

UNITED STATES OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA

BRIEF FOR THE UNITED STATES

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IN THE UNITED STATES COURT OF APPEALS FOR THE
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No. 18828

WILLIAM BRUCKER,

Appellant,

v.

UNITED STATES OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA

BRIEF FOR THE UNITED STATES

JURISDICTIONAL STATEMENT

Appellant brought this action against the United States under the Federal Tort Claims Act (28 U.S.C. 1346(b)), asserting liability for the injuries he received as a member of the Castle Air Force Base Aero Club while riding in an airplane which he had rented from that Club, which was being piloted by another member of the Club (R. 26-29, 45-48).[1/] The asserted liability was based solely upon the alleged negligence of

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1/ "R." references are to Volume I of the Record as reproduced in this Court. "Tr." references are to the transcript of testimony, which forms Volumes II and III of the Record here.

the pilot of the airplane (R. 58-61). After a full trial the district court found that the pilot was not flying the airplane as an agent of the Club or as an agent or employee of th United States, and entered a judgment dismissing the complaint from which this appeal is taken (R. 76-80, 83).

The jurisdiction of this Court rests upon 28 U.S.C. 1291.

STATEMENT OF THE CASE

1. The basic facts. The basic facts were found by the district court (R. 76-79), and are now largely undisputed.

The Castle Air Force Base Aero Club was organized under the provisions of Air Force Regulations (AFR) 34-14 and 176-1, in 1957, as a non-appropriated fund instrumentality of the United States (Ex. E). Its principal purpose was to provide an opportunity for Air Force personnel and their dependents "to engage in flying as a recreational activity" and thereby to encourage the acquisition and development of aeronautical skills (R. 77, Finding IV; R. 14, AFR 34-14, para. 2, infra, p. 2a). Membership in the Club was voluntary and was open to civilian employees of the Air Force, retired military personne and their dependents, as well as to active duty personnel and their dependents (R. 14, AFR 34-14, para 4, infra, pp. 2a-3a; Ex. 2, Ex. H, Article III A, infra, p. 5a). The Club had its own constitution and by-laws (Ex. 2, Ex. H, infra, pp. 5a-9a), and elected its own officers (R. 77, Finding IV). The Club wa designed to be self-supporting financially, receiving its income from initiation fees, membership dues, and fees for the

rental of its airplanes (Ex. 2, Ex. H, Article V and III, infra, pp. 6a, 5a). The powers and business of the Club was exercised and controlled by an executive board of six members, elected by members of the Club at the annual meeting. The President of the Club, who was to serve without compensation, had general charge of the business of the Club, subject to the advice and control of the executive board, and was responsible for its operation. In particular, he was responsible for determining the suitability of equipment and qualifications of members for all flight operations (Ex. 2, Ex. H, para. 4, infra, p. 8a).

The Club's facilities were located at Buller Field, approximately three miles from Castle Air Force Base (Tr. 125-126). Members of the Club who wished to fly would rent the airplane on an hourly basis from the Club (R. 77, Finding II; Tr. 123). Members of the Club participated in its activities on their own time, i.e., only while they were off duty (Tr. 55, 58, 74-75).

For those members who wished to have flying instruction, the Club maintained a list of flight instructors at its headquarters. The list contained the names of persons who had Federal Aviation licenses to give civilian flying instruction, and who had been designated by the Club to instruct its members in Club airplanes (R. 77-78, Finding V; Tr. 129). Some of the instructors were not members of the Club. The members selected

the instructors, engaged them privately, and were allowed to make their own financial arrangements with them (Tr. 131-132). It was the practice for a student member to pay the instructor he selected $3.00 per hour for instructions (R. 78, Finding V).

The Club also maintained a roster of "check" pilots, who were licensed pilots, authorized by its rules to "check out" other licensed pilots in airplanes they had not previously flown, in order to comply with the Club's rule that a pilot must be checked out in an airplane he had not previously flown before flying it alone (R. 78, Finding VI; Tr. 164). Check pilots, like other members who held licenses, were authorized to fly Club airplanes with passengers (Tr. 165-166).

In 1959, appellant was an enlisted man in the United Stat Air Force, with the rank of technical sergeant, assigned to Castle Air Force Base as a fire fighting supervisor (R. 76-77, Finding I). He had previously become a member of the Aero Club, and had taken instruction from civilian flying instructo on the Club's list of qualified instructors, as well as from a Master Sergeant Graves, who was both the President of the Club and a qualified flying training instructor (R. 77, 78-79, Findings IV and VII; Tr. 131-132). On May 28, 1959, he flew solo for the first time (Tr. 61).

On Saturday afternoon, June 6, 1959, after being released from fire alert duty, appellant went out to Buller Field in the hope that he could take another solo flight under Sgt.

Graves' supervision (Tr. 75). When he learned that Sgt. Graves was not at the field, he asked Lieutenant Maurice Hammack, who was also off-duty, to accompany him on a flight (R. 76-77, Finding I). Hammack was a member of the Club and a rated military pilot (R. 77, 78, Findings I and VII). He was not a qualified instructor, as appellant knew, and his name was not upon the Club's list of qualified instructors (R. 79, Finding VII; Tr. 118); but he held a civilian commercial pilot's license, and was a listed check pilot and club member authorized to fly with other persons in the airplane (Tr. 163, 165-166). Sgt. Graves was apparently unaware of the proposed flight (Tr. 73-77).

When Hammack agreed to appellant's suggestion, appellant rented an Aeronca Champion airplane, owned by the Club, on an hourly basis for $3 an hour (R. 77, Finding II; Tr. 76, 123-124). They took off, with Lt. Hammack in the rear (pilot's) seat, and appellant in the front seat (R. 77, Finding III; Tr. 76-82). At approximately 3 p.m., while Hammack was flying the airplane and attempting to demonstrate to appellant a low altitude, down wind, power off, forced landing procedure, the airplane crashed, and appellant sustained injuries (R. 77, 78, Findings III and VII).

2. District court proceedings. After his state court action against Hammack, Graves and the Castle Air Force Base Aero Club had been removed to the district court on the ground

that the Club was a Federal instrumentality, appellant brought this action against the United States under the Federal Tort Claims Act, 28 U.S.C. 1346(b), 2671, et seq., alleging that hi injuries resulted from the negligent flying of the airplane by Hammack and claiming $273,000 in damages (R. 45-48). The pre-trial conference order specified that appellant was seeking recovery solely on the basis of the asserted negligence of "Hammack as agent or employee" of the United States and the Aero Club; and jurisdiction was asserted solely on the ground that Hammack was flying the airplane within the scope of his employment (R. 58, 59). The parties agreed upon many of the facts set forth above (R. 59-61). The Government did not contest the negligence of Hammack, but asserted, inter alia, (1) that Hammack was not acting as an employee of the United State within the scope of his employment; (2) that appellant was guilty of contributory negligence or had assumed the risk of Hammack's conduct; (3) that the California Aircraft Guest Statute was applicable; or (4) that appellant's participation in the flight was incident to his service in the Air Force (R. 63).

At trial, appellant testified on his own behalf. He did not testify, or offer any other direct evidence, that Hammack was employed by the Aero Club, but impliedly conceded that Hammack did not work at the Club (Tr. 124-125). He also admitted that neither Hammack nor Graves had told him that Hamm

was a qualified instructor, and that he had no reason to believe that Hammack was a qualified instructor (Tr. 118-119, 127-128). Although he asserted that he considered himself a student and Hammack an instructor for purposes of the flight (Tr. 132-135), he also conceded that members were free to select their flying instructors and to make their own financial arrangements with them; and that he had paid his instructors $3 per hour, but had not paid Hammack anything on their prior flight together (Tr. 131-132). Appellant testified that on one prior occasion Sgt. Graves had authorized Lt. Hammack to fly with appellant at a time when Sgt. Graves himself was unable to give instructions (Tr. 63-66). Appellant offered no evidence to indicate that Sgt. Graves had authorized the flight which gave rise to the injuries. Indeed, his testimony plainly indicated that Sgt. Graves was wholly unaware of the flight in question until after it had taken place (Tr. 74-81).

Sgt. Graves testified unequivocally that Lt. Hammack was on no pay status with the Aero Club (Tr. 162). He also testified that Hammack was a military pilot, who was on temporary duty at Castle Air Force Base for three months, and that he had a civilian commercial pilot's license, and that he was an authorized check pilot (Tr. 163). He contradicted appellant's charge that he had made a back-dated entry in appellant's log, and testified that he had not authorized Lt. Hammack to give instruction to appellant, and that he did not recall any telephone

conversation in which he had authorized appellant to fly with Hammack (Tr. 153-155); and that it was proper for any rated pilot, including a "check pilot," to take a student for a ride so long as the rated pilot does the flying (Tr. 165).

The district court found that Hammack's negligence was the proximate cause of appellant's injuries, that there was no mechanical difficulty with the airplane, and that there was no negligence by Sgt. Graves in his management of the Aero Club (R. 78, Finding VII). The court also found that, althoug Sgt. Graves had authorized a prior flight by Lt. Hammack with appellant, he had not authorized the flight on the day in question (R. 78-79, Finding VIII); and that, although there was no express financial arrangement between appellant and Hammack, there was an implied obligation on appellant's part to pay Hammack a $3 per hour fee (R. 79, Finding IX). The court found that the flight was an independent recreational activity, and ruled that appellant's injuries did not arise out of or in the course of military duty, within the exception of the Tort Claims Act announced in Feres v. United States, 34 U.S. 135 (R. 79, Conclusion II). Lastly, the court found that Hammack was not acting as an agent of the Club or the United States at the time of the flight in question (R. 79, Finding X).

Based upon the foregoing findings and rulings the district court concluded that the appellant's injuries were caused solel

by the negligence of Hammack, and that he was not flying the airplane as an employee or agent of the United States or its instrumentality, the Castle Air Force Base Aero Club (R. 80, Conclusions I, II, III). Accordingly, the court ruled that appellant's action could not be maintained against the United States, under the Federal Tort Claims Act (28 U.S.C. 1346(b)) which permits suits against the Government only for negligent acts or omissions of its employees acting within the scope of their employment (R. 80, Conclusion VII); and entered a judgment dismissing appellant's complaint for want of jurisdiction over the United States (R. 80). From that judgment, appellant takes this appeal (R. 83).

QUESTIONS PRESENTED

1. Whether the district court was clearly erroneous in finding that the pilot of the airplane was not an agent of the Aero Club, and that the president of that Club was not negligent.

2. Whether the district court erred in ruling that the pilot of the airplane was not an employee of the Aero Club within the meaning of the Federal Tort Claims Act.

3. Whether appellant can raise a factual issue for the first time in this Court, when he stipulated, in a pre-trial conference order, that the issue was not in the case.

STATUTES AND REGULATIONS INVOLVED

1. The Federal Tort Claims Act, 28 U.S.C. 1346(b), 2674, provides in pertinent part:

> §1346(b). Subject to the provisions of chapter 171 of this title, the district courts, * * * shall have exclusive jurisdiction of civil actions on claims against the United States, for money damages, accruing on and after January 1, 1945, for injury or loss of property, or personal injury or death caused by the negligent or wrongful act or omission of any employee of the government while acting within the scope of his office or employment, under circumstances where the United States, if a private person, would be liable to the claimant in accordance with the law of the place where the act or omission occurred.
>
> * * * * * *
>
> §2671. Definitions
> As used in this chapter and sections 1346(b) and 2401(b) of this title, the term --
> "Federal agency" includes the executive departments and independent establishment of the United States, and corporations primarily acting as, instrumentalities or agencies of the United States but does not include any contractor with the United States.
>
> "Employees of the government" includes officers or employees of any federal agency, members of the military or naval forces of the United States, and persons acting on behalf of a federal agency in an official capacity, temporarily or permanently in the service of the United States, whether with or without compensation.
>
> "Acting within the scope of his office or employment," in the case of a member of the military or naval forces of the United States, means acting in line of duty.
>
> * * * * * *

§2674. Liability of United States.

The United States shall be liable, respecting the provisions of this title relating to tort claims, in the same manner and to the same extent as a private individual under like circumstances, but shall not be liable for interest prior to judgment or for punitive damages.

2. The pertinent provisions of the Air Force Regulations and the Constitution and By-Laws of the Castle Air Force Base Aero Club are set forth as an Appendix to this brief, infra, pp. 1a-9a.

ARGUMENT

Introduction and Summary

The Aero Clubs of the various Air Force installations which are organized as non-appropriated fund activities[2] are instrumentalities of the United States. Their employees may be considered employees of the United States for purposes of the Federal Tort Claims Act.[3] However, a member of such a club who uses its airplanes is no more an employee of the club, within the meaning of that Act, than a purchaser of goods at a post exchange is an employee of the exchange, or a member of an officers' club is an employee of the club United States v. Hainline, 315 F. 2d 153 (C.A. 10, 1963), 375 U.S. 895 Similarly, Air Force personnel flying club airplanes on their own time (while off duty) are not acting within the scope of their military employment, within the meaning of the Federal Tort Claims Act. Ibid.

Apparently recognizing and accepting these principles,[4] appellant bases his appeal upon the theory that Hammack was

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[2] Some Aero Clubs are organized as private associations See AFR 34-14, ¶ 1c, infra, pp. 2a . Such clubs would not be instrumentalities of the Government.

[3] United States v. Holcombe, 277 F. 2d 143 (C.A 4, 1960); Accord: Forfari v. United States, 268 F. 2d 29 (C.A. 9, 1959), certiorari denied 361 U.S. 902; Rizzuto v United States, 298 F. 2d 748 (C.A. 10, 1961).

[4] If Hammack had been flying the airplane within the scope of his employment as an employee (officer) of the Air Force, appellant who was in the same status, could not at any rate recover under the Tort Claims Act because the flight would then have been incident to appellant's military duty, and his claim for damages for personal injuries not actionable under the Tort Claims Act. Feres v United States, 340 U.S. 135.

.ying the airplane as an employee of the Castle Air Force
ıse Aero Club, because he was a "check pilot" and upon the
'ound that the president of the club negligently authorized
.m to fly a club airplane.

Apart from the fact that all duly licensed members were
ıthorized to fly club airplanes, the trouble with appellant's
ıeory is that there is no evidence in the record to indicate
ıat Hammack was employed by the Club or that check pilots
ere club employees; and the uncontroverted evidence was that
e was a member of the Club, and was on no pay status of any
.nd with the Club. Moreover, the record disclosed no
ttributes of an employer-employee relationship between Hammack
ıd the Aero Club. The district court was therefore entirely
orrect in finding that Hammack was not an agent of the Club,
ıd in ruling that he was not flying the airplane as an employee
the United States. Appellant's contention, raised for the
.rst time in this appeal, that the president of the Aero Club
ıs negligent in authorizing Hammack to fly with appellant, is
oreclosed by the pre-trial stipulation and order, and the
ıstrict court's finding that he was not negligent.

I

THE PILOT, WHOSE NEGLIGENCE WAS THE SOLE PROXIMATE CAUSE OF APPELLANT'S INJURIES, WAS NOT FLYING THE AIRPLANE AS AN EMPLOYEE OF THE UNITED STATES OR ITS INSTRUMENTALITY, THE CASTLE AIR BASE AERO CLUB.

A. The Record Fully Supports The District Court's Finding That Hammack Was Not An Agent Of The Castle Air Force Base Aero Club.

The district court found as a fact that "Lt. Hammack was not acting as an agent of the club and hence not an agent of the Government at the time of the flight in question" (R. 79, Finding X). Appellant challenges the finding on the grounds that it is merely a conclusion and is incorrect We show here that the court's finding is fully supported by the evidence, which shows that Hammack was flying the airplane on behalf of appellant and that if he was anyone's agent, he was an agent of appellant.

1. The evidence concerning Lt. Hammack's status in relationship to the Aero Club may be briefly recapitulated here. It has, of course, been conceded from the beginning of the litigation that Hammack was a member of the Aero Club (R. 5,27). There was virtually no evidence to indicate that he was also an employee, and there was positive evidence that he was not. Appellant himself testified that Lt. Hammack was not a full time employee of the Aero Club (Tr. 124-125), and submitted no testimony, club records or any other form of evidence to indicate that Hammack was employed by the Club for any purpose or in any capacity. Indeed, when asked on cross-examination if Hammack "worked at the Club," appellant replied (Tr. 125):

Well, I don't believe that anybody actually worked at the Club full time, except maybe Sgt. Tilson * * *.

nd when pressed as to whether Sgt. Graves or anybody else as working for the Club part time, appellant merely replied nat Sgt. Graves was president of the Club (Ibid.). Appellant's vn testimony, therefore, strongly suggests that he recognized nat Hammack was not employed by the Club, either on a full part time basis.

On direct examination of the president of the Aero Club, gt. Graves, counsel for appellant carefully refrained from sking whether Hammack was employed by the Club in any capacity Tr. 151-159). On cross-examination, Sgt. Graves testified nequivocally that Hammack was not paid by the Club for any ork and was not on any pay status with the Club (Tr 162). n context, the clear inference from Sgt. Graves' testimony as that Hammack was not employed by the Club in any capacity Ibid.)

The record discloses that Hammack was flying the airplane s a member of the Aero Club, under an agreement with appellant. ppellant testified that he went to Buller Field in the hopes f his finding his instructor (Sgt. Graves) there, so that he ould have further instruction (Tr. 75). When he discovered nat his instructor was not there, he requested Hammack to ccompany him on a flight and, when Hammack agreed, appellant ented the airplane from the Aero Club, and they took off Tr. 75-76; R. 60). It was the custom and practice for students

and passengers to pay $3 an hour to the pilot in similar circumstances, and the district court found that appellant was impliedly obliged to pay Hammack $3 an hour for this trip (R. 79, Finding IX). From these conceded facts, it seems clear that Hammack was engaged by appellant to accompany him on the flight. If Hammack was anyone's agent in flying the airplane, therefore, the record discloses that he was the agent of appellant, and not an agent of the Aero Club.

Appellant relies upon the fact that Hammack was on the Aero Club's list of authorized check pilots (Tr. 163, R. 60) to support his argument that Hammack was acting as agent for the Aero Club in flying the airplane (Brief for Appellant, pp. 12, 14, 18-19). But there was no showing that pilots, who were on the Club's list of authorized check pilots flew, the airplanes as agents of the Club. On the contrary, the evidence shows that the student and passenger members of the Club privately selected and engaged the flight instructors and check pilots they wished to have and were free to make their own financial arrangements with them (Tr. 131-132). Indeed, as appellant testified, one of his instructors was the proprietor of "Bob Swann's Flying Service," while a second instructor was an employee of that organization (Tr. 59-60). There was a total absence of proof of any contractual or pay relationship between the Aero Club, on the one hand, and the flight instructors and check pilots on the other. The clear implication of the record is that check pilots and flight instructors were engaged by the student and passenger members,

s independent contractors or employees; and that, as such, hey were agents of the members who engaged them and/or heir private employer and were not agents of the Aero Club.

Appellant also attempts to rely upon the fact that gt. Graves had previously authorized a flight in which Hammack as to accompany appellant (Brief for Appellant, pp. 18-19). t is, of course, true that Sgt. Graves, as president of the ero Club, was authorized to approve or disapprove particular lights. But as the by-laws expressly state, his decision in hat regard was to be based upon the "suitability of all quipment" and the qualifications of the members for the type f flight involved (By Law, ¶ 4, b, infra, p.8a). His uthorization of the prior flight therefore reflected only is view that Hammack was qualified to fly the airplane with ppellant in it. The record does not support the view that gt. Graves authorized Hammack to fly the airplane on behalf f the Club, or as an agent of the Club (Tr. 62-65, 153-155, 65-167).

Rule 52(a) of the Federal Rules of Civil Procedure rovides, of course, that the district court's "findings of act shall not be set aside unless clearly erroneous, and due egard shall be given to the opportunity of the trial court o judge of the credibility of the witnesses." An appellate ourt may set aside a district court finding as "clearly rroneous," only if the reviewing court on the entire record s left with the firm conviction that a mistake has been committed.

United States v. United States Gypsum Co., 333 U.S. 364, 395. An appellant challenging factual findings has a very heavy burden on appeal, which the Supreme Court has recently described as "an almost insurmountable burden." International Boxing Co. v. United States, 358 U.S. 242, 252. As this Court has recently ruled (Lundgren v. Freeman, 307 F. 2d 104, 113):

> We are bound by Rule 52(a) F.R. Civ.P., which provides that: "findings of fact shall not be set aside unless clearly erroneous * * *." Therefore, we may not substitute our judgment if conflicting inferences may be drawn from the established facts by reasonable men, and the inferences drawn by the trial court are those which could have been drawn by reasonable men.

Accord: Stacher v. United States, 258 F. 2d 112, 118 (C.A. 9, 1958) (district court findings entitled to "all favorable inferences").

On the facts disclosed from this record it is doubtful that a reasonable man could infer that Hammack was flying the airplane as an agent of the Aero Club. Certainly, the district court's finding that he "was not acting as an agent of the Club" (R. 79, Finding X) is reasonable and fully supported by the evidence of record. Accordingly, it is not "clearly erroneous" and should be accepted by this Court Lundgren v. Freeman, supra; United States v Grissler, 303 F. 2d 175, 176 (C.A. 9, 1962). And since Hammack was not an agent of the Aero Club, he was not acting "on behalf of" the Aero Club, was not an employee of the United States within the meanin of the Tort Claims Act. 28 U.S.C. 2671, supra, p 10 .

B. The District Court Ruling that Hammack Was Not An Employee of the Aero Club Is, at Any Rate, Correct.

Because the record fully supports the district court's inding that Hammack was not flying the airplane as an agent the Aero Club, and it is conceded that he was not acting ithin the scope of his military employment, that finding is, believe, dispositive of appellant's contention that the nited States is liable for his negligent conduct. For the ake of completeness, however, we show here that appellant ould not be able to prevail even if that finding could be onsidered "clearly erroneous."

The Tort Claims Act permits suits against the United tates only for the negligence of its employees. 28 U.S.C. 46(b), supra, p. 10 . Even apart from the district ourt's finding that Hammack was not flying the airplane s an agent of the Aero Club, the other factors necessary o a showing of an employer-employee relationship were wholly bsent in the relationship between the Aero Club and Hammack. he district court's conclusion that Hammack was not acting within the scope of any office or employment at the time the accident in question" (R. 80, Conclusion VI) is herefore correct, regardless of whether Hammack was acting s an agent of the Aero Club.

Although the state law governs the determination of hether an employee is acting "within the scope of his mployment" under the Federal Tort Claims Act (28 U.S.C.

1346(b)),[5] the question of whether a person is an employee within the meaning of that Act (28 U.S.C. 1346(b) and 2671) is determined by federal law. Pattno v. United States, 311 F. 2d 604 (C.A. 10, 1962), certiorari denied, 373 U.S. 911; United States v. Hainline, 315 F. 2d 153 (C.A. 10, 1963), certiorari denied, 375 U.S. 895. Accord: United States v. Wendt, 242 F. 2d 855 (C.A. 9, 1957). Accordingly, our discussion of this issue is in terms of Federal law.[6]

It has long been a basic principle of agency law that the putative employer's right to control and direct the manner in which work is to be done is an essential element in determining whether an individual is an employee of another for purposes of vicarious tort liability. As the Supreme Court has ruled, Singer Manufacturing Co. v. Rahn, 132 U.S. 518, 523 (1889):

> * * * the relation of master and servant exists whenever the employer retains the right to direct the manner in which the business shall be done, as well as the result to be accomplished * * *

This rule, which is, of course, based upon the elemental unfairness of imposing liability on one person for the activities of another over which he has no control, was

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[5] Williams v. United States, 350 U.S. 587 (1955); Callaway v. Garber, 289 F. 2d 171 (C.A. 9, 1961).

[6] Federal law and the law of California both adopt the tests of the Restatement, Agency 2d Sec. 220, and appear to be identical on this matter. Compare Isenberg v. California Employment State Co., 30 Cal. 2d 34, 180 P. 2d 11, 15; with Strangi v. United States, 211 F. 2d 305, 308 (C.A. 5, 1954).

mbodied in the Federal Tort Claims Act.[7/] In the absence of uch a right in the United States or its agencies to control he conduct of the asserted employee, the courts have held that here is no employer-employee relationship within the meaning f the Act and have refused to impose liability upon the nited States. E.g., Strangi v. United States, 211 F. 2d. 305, 07-308 (C.A. 5, 1954); Harris v. Boreham, 233 F. 2d 110 C.A. 3, 1956); Lavitt v. United States, 177 F. 2d 627 (C.A. , 1949). As the Fifth Circuit stated in Strangi (211 F. 2d t 307):

> The distinction between the master-servant and independent contractor relationship lies largely in the degree of control or right of control retained by the employer over the details of the work as it is being performed * * *

This vital "control" factor is missing here. There as absolutely no showing that the Club or any of its officers ad the right to tell Hammack where, how, or when to fly the irplane, or whether he should fly it at all. Indeed, appellant's wn testimony makes it clear that the Aero Club had no such ights. It was conceded that appellant requested Hammack to ccompany him on the flight in question (R. 60). From ppellant's own testimony it was also clear that Hammack was ree to refuse appellant's request and that the arrangements or the flight were exclusively between Hammack and appellant

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/ In adopting Pub. L. 86-740, 74 Stat. 178, 32 U.S.C. (Supp. I) 715, Congress based its decision that the United States hould not be liable for the negligence of members of the ational Guard upon the absence of Federal control over the ational Guard while in state service. Sen. Rept. 1502, 86th ong., 2d Sess., p. 4; H. Rept. 1928, 86th Cong., 2d Sess., p. 4.

(Tr. 75-76, 131-133). The time, length and itinerary of the trip were obviously matters to be determined between Hammack and appellant (Ibid.). Since Hammack was on his own time, free to fly or not as he saw fit, the Aero Club obviously did not have the right to control the details of his conduct which is a prerequisite to the imposition of vicarious tort liability under the Tort Claims Act.

Other factors normally present in the employer-employee relationship are wholly absent in the relationship between the Aero Club and Hammack. See, Restatement, Agency 2d, Sec. 220; Strangi v. United States, 211 F. 2d 305, 307-308. The Aero Club did not pay Hammack in any way (Tr. 162), and the only remuneration Hammack could expect for the flight would come from appellant (R. 79). Compare, Restatement, Agency 2d, Sec. 220(g). As a pilot, Hammack had a skilled and distinct occupation, and the record strongly suggests that instructors and check pilots in the area acted as specialists, without supervision.[8/] Id., Sec. 220(b), (c) and (d). The airplane for the flight in question was rented and furnished by appellant (R. 77, Finding II). Id., Sec. 220(e). Hammack appears to have been employed only for the duration of the flight (Tr. 131-132). Id., Sec. 220(f). And there is nothing in the record which suggests that giving members rides was a part of the regular business of the Aero Club, or that the officers of the Club and/or Hammack believed they were creating an employer-employee

8/ One of appellant's instructors was the independent proprietor of a local flying service (Tr. 59-60).

relationship. Id., Sec. 220(h) and (i).

In short, appellant has failed to prove any of the elements necessary to showing that Hammack was an employee of the Aero Club. On this record, therefore, the district court's ruling (R. 80, Conclusion VI) that he was not flying the airplane as an employee of the Club must be sustained.

II.

ANY ISSUE AS TO THE NEGLIGENCE OF THE PRESIDENT OF THE AERO CLUB WAS FORECLOSED BY THE PRE-TRIAL ORDER; AND THE DISTRICT COURT'S FINDING THAT HE WAS NOT NEGLIGENT IS FULLY SUPPORTED BY THE EVIDENCE

In the district court appellant based his case solely upon the theory that Hammack was an employee of the Aero Club, so that the United States was liable for his negligent piloting of the airplane. Nevertheless, appellant now asserts on appeal that the district court erred in failing to find negligence on the part of Sergeant Graves, the President of the Club (Brief for Appellant, pp. 15-17, 19).

A. The short answer to appellant's assertion is that appellant has waived the issue. The Pre-Trial Conference Order stated that the action was one for damages based upon the "alleged negligence on the part of defendant *** on the part of MAURICE H. HAMMACK as agent or employee ***" (R. 58). Similarly, jurisdiction was based solely upon the ground that Hammack was acting as an employee of the Government, through the Aero Club (R. 59). While the negligence of Hammack was not contested,

there was no reference to possible negligence on the part of Graves in the facts which were admitted or not contested, or included in "the following issues of fact, and no others, remain to be litigated upon trial" (R. 59-61). Similarly, whil one of the listed "issues of law" was whether Hammack's negligence was a proximate cause of appellant's injuries, there was no reference to any casual relation between appellant's injuries and possible negligence on the part of Graves among "The following issues of law, and no others, remain to be litigated (R. 63-64). Indeed there was no reference to possible neglige on the part of Graves in the entire pre-trial order (R. 58-65) In addition to specifying the only issues of fact and law whic remained to be tried, the order specified that it would "gover the course of the trial of this cause, unless modified to prevent manifest injustice" (R. 64-65). It was signed "Approved as to Form and Content" by counsel for both parties (R. 65).

The order formulated and narrowed the issues between the parties. The Government, for example, agreed not to contest the asserted negligence of Hammack, while appellant limit his claim to the asserted negligence of Hammack. By specifyin the issues which remained to be litigated, "and no others," the order clearly foreclosed any claim on appellant's part bas upon assertions of negligence on the part of those other than Hammack.

One of the basic purposes of pre-trial conferences pursua to Rule 16 of the Federal Rules of Civil Procedure is, of cour

to facilitate "The simplification of the issues" in dispute between the parties. Rule 16, Fed. R. Civ. P.; Fowler v. Crown Zellerback Corp., 163 F. 2d 773 (C.A. 9, 1947). Where the pre-trial conference order frames and limits the issues with the agreement, or without the objection, of the parties, therefore, the order "controls the subsequent course" of the litigation,"unless modified at the trial." Rule 16, Fed. R. Civ. P. Unless the order is so modified, a party is therefore precluded from raising an issue at trial which was omitted from the pre-trial order. First Federal Savings & Loan Assn. v. United States, 295 F. 2d 481 (C.A. 9, 1961); Fowler v. Crown Zellerback Corp., supra. 1A Barron & Holtzoff, Federal Practice, Sec. 473, pp. 844-851.

These principles are controlling here. Having stipulated and agreed that his case was based solely upon the asserted negligence of Hammack, appellant is in no position to urge district court error for refusing to find negligence on the part of Graves. In similar circumstances, this Court has recently stated (First Federal Savings & Loan Assn. v. United States, supra, 295 F. 2d at 482-483):

> We need not comment upon the impropriety of this Court considering reversal of a district court judgment for failure to pass upon an issue never framed for consideration by that court.

It would, we think, be equally improper for this Court to consider a challenge to the district court judgment in this case,

for its refusal to find that Graves was negligent, when appellant never contended in that court that he was negligent, and the issue was never framed for consideration by that court.

It is, of course, true that evidence was admitted upon which a finding of negligence or no negligence on the part of Graves could have been based (see infra, p. 27). But that testimony, admitted over objection by Government counsel was to show the circumstances under which Hammack made his flight (R. 65), and was also pertinent to show the relationship between Hammack and the Aero Club. For that reason "it cannot be argued that the receipt of the evidence * * * enlarged the issues" as framed by the pre-trial order. First Federal Savings & Loan Assn. v. United States, supra, 295 F. 2d at 482.

After the close of the testimony, and the informal ruling of the court that Hammack was not acting as an employee of the Aero Club, counsel for appellant requested the court to "make a ruling on the issue of ostensible agency as create by Sergeant Graves in Lieutenant Hammack" (Tr. 221). In the resulting discussion, the court stated, "I don't find any negligence on the part of Sergeant Graves" (Tr. 222). Appellant apparently did not object to that proposed finding (Tr. 222; R. 70-72). The formal finding to the same effect was entered (R. 78, Finding VII).

Having stipulated in the pre-trial order to the effect that there was no issue pertaining to possible negligence on the part of Graves, and having failed to object to the proposed finding that Graves was not negligent, appellant should not now be heard to complain that the district court erred in making the finding. His contentions in this regard should not be considered by the court. First Federal Savings & Loan Assn. v. United States, 295 F. 2d 481 (C.A. 9, 1961).

B. At any rate, the district court found specifically that Sgt. Graves was not negligent in his management of the affairs of the Aero Club (R. 78, Finding VII). Contrary to appellant's contention (Brief for Appellant, p. 14), there is no ambiguity in the finding and no reasonable basis for doubt as to its meaning. After ruling, in accordance with a request of counsel for appellant, that Graves had authorized a prior flight of Hammack with appellant (Tr. 221-222), the court stated (Tr. 222):

> I don't find any negligence on the part of Sergeant Graves.

It is therefore clear that the district court found that Graves was not negligent in any pertinent respect, including his authorization to Hammack to fly with appellant approximately a week before the flight (Tr. 221-222).

The only evidence upon which a contrary finding could have been based was the testimony of appellant himself. Appellant testified that on May 29, 1959, when Sgt. Graves was unable to

keep an appointment with him for flying instruction, Graves spoke to Hammack on the telephone, Hammack took appellant in an airplane, and let him fly solo, and that Sgt. Graves later made a false, back-dated entry in appellant's log book, in which he gave appellant credit for instruction time, and listed himself as instructor (Tr. 62-73). From this testimony appellant infers that Graves authorized Hammack to act as appellant's instructor (Brief for Appellant, pp. 14, 19), although it was stipulated in the pre-trial conference order that Hammack accompanied appellant "as a check pilot" (R. 60).

Sgt. Graves forcefully denied that he had ever made any back-dated entries in appellant's log, and testified that he had never authorized Hammack to give flight instruction to appellant (Tr. 153-155). This testimony was in no way shaken on examination by counsel for appellant (Tr. 165-167, 167-170).

Having had the opportunity to observe the demeanor of the witnesses and to judge their credibility, the district judge was in a position to determine which of the inconsistent stories to believe. And the district court's resolution of conflicts in testimony cannot, of course, be disturbed here. Rule 52(a) Fed. R. Civ. P.; Soby v. Johnson, 270 F. 2d 193 (C.A. 9, 1959).

Appellant concededly did not hear Sgt. Graves authorize Hammack to give him instruction, but merely deferred the authorization from later conduct, while Sgt. Graves expressly and

emphatically stated that he had not given any such authorization. Moreover, the parties stipulated that Hammack accompanied appellant "as a check pilot" (R. 60). In light of this record, the district court's finding that Sgt. Graves was free from negligence is not only reasonable, but is supported by the preponderance of the evidence.

CONCLUSION

For the foregoing reasons, the judgment of the district court should be affirmed.

Respectfully submitted,

JOHN W. DOUGLAS,
Assistant Attorney General,
FRANCIS C. WHELAN,
United States Attorney,
MORTON HOLLANDER,
DAVID L. ROSE,
Attorneys, Department of Justice,
Washington, D.C. 20530,
Attorneys for Appellee.

March 1964.

CERTIFICATE

I certify that, in accordance with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

DAVID L. ROSE
Attorney for Appellee.

APPENDIX

1. Air Force Regulation AFR 34-14, provides in pertinent part:

*AFR 34-14
1-4

AIR FORCE REGULATION NO. 34-14

DEPARTMENT OF THE AIR FORCE
Washington, 14 April 1959

Personnel Services

AIR FORCE AERO CLUBS

This regulation authorizes commanders to establish Air Force aero clubs organized as sundry fund activities, tells them how to do so, and states what controls commanders should place on operation of the clubs. Its provisions, together with other Air Force regulations cited herein and applicable parts of Civil Aviation Regulations published by the Federal Aviation Agency (FAA), apply to Air Force aero clubs worldwide.

1. SPECIFIC APPLICABILITY.

a. Within the continental United States, commanders will follow the policies and operational principles prescribed by this regulation and other regulations cited above.

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* This regulation supersedes AFR 34-14, 9 February 1956.
OPI:AFPMP
DISTRIBUTION:B

b. Outside the continental United States, commanders may augment this regulation in any manner to comply with the rules and regulations of the country in which they are located, provided they do not deviate from the intent of this regulation.

c. This regulation does not apply to aero clubs established as private associations (see AFR 176-1).

2. PURPOSE OF AERO CLUBS. Aero clubs are designed to stimulate an interest in aviation; to provide authorized personnel with an opportunity to engage in flying as a recreational activity; and to encourage and develop skills in aeronautics, navigation, mechanics, and related aero sciences useful to the Air Force mission.

3. HOW TO ESTABLISH AERO CLUBS.

a. Major air commanders may approve the establishment of aero clubs as sundry fund activities in keeping with AFR 176-1 to operate as instrumentalities of the Federal Government under the auspices of the Air Force.

b. An Air Force aero club must organize under a constitution or charter and by-laws which provide for its operati and dissolution consistent with this and other other(sic) applicable regulations.

c. An Air Force aero club may carry the name of its base location; for example, a club formed at Randolph Air Force Base may be known as the "Randolph Air Force Base Aero Club."

d. Local policies and regulations may be issued to insure that clubs operate smoothly, efficiently, and properly, provided the policies and regulations are consistent with this and other applicable regulations.

4. MEMBERSHIP IN AERO CLUBS. Membership in an Air Force aero club shall be voluntary. Active membership will be limited to active duty military personnel of the Armed Forces. Associate membership may be extended to the following:

a. Dependents of military personnel.

b. Retired military personnel and their dependents.

c. Civilians employed by the Air Force or by non-appropriated fund activities of the Air Force.

d. Military personnel of foreign governments on duty with the Department of Defense.

5. ASSIGNMENT OF PERSONNEL. Responsibilities for adequate supervision and control of clubs may require limited utilization of personnel to perform the command functions cited in the following paragraph. However, military and civilian personnel, paid from appropriated funds, will not be assigned to clubs specifically to perform maintenance, instructional and general administration, and operational duties. As sundry fund activities, clubs are expected to operate on a self-sustaining basis; therefore, provisions of AFR 176-1, on the use of military personnel are not applicable.

6. COMMAND SUPERVISION OF CLUB OPERATION. Commanders will supervise club operation to insure that:

a. Appropriate operational and administrative procedures are established and followed to insure maximum safety of flight. The rules and regulations of the FAA should be supplemented, if required, based on the flying experience available within the club.

b. The club maintains an effective air-ground safety program.

c. The club operates on a self-supporting basis in a businesslike manner to assure financial stability, and club fund accounting procedures are consistent with those prescribed by AFM 177-4.

d. Authorization is granted members of Air Force aero clubs to pilot USAF aircraft on loan, provided:

(1) Member holds currently effective airman's certificate issued by FAA for type of aircraft and operation involved, or

(2) Member has not qualified for FAA rating, but is undergoing student pilot training in accordance with current operational procedures prescribed by FAA and the aero club concerned.

e. Coordination and working relationship is established with the local FAA inspector to insure maximum assistance for club operations.

f. Hobby shop facilities and other equipment are made available, when possible, to assist club members in maintaining and repairing aircraft.

g. Sale of petroleum products is in accordance with AFR 67-147.

h. Authorization for use of Air Force installations by aero club aircraft is determined by paragraphs 2a(1) and 11, AFR 55-20, 26 February 1959.

* * * * * * *

11. INSURANCE REQUIRED. Provisions of AFR 176-8 give guidance with respect to public liability insurance coverage for Air Force aero clubs, including insurance covering public property damage, public bodily injury, and passenger bodily injury. However, the provisions of that regulation are not applicable to:

a. Individually owned aircraft which may be used by club members. In such cases commercial insurance coverage, as required by AFR 87-7, will be provided by the individual.

b. Hull insurance on aircraft owned by the aero club or individual club members. Hull insurance should not be carried on aircraft on loan from the Air Force. Title to the aircraft rests with the United States Government; therefore insurance companies do not have salvage rights to the aircraft.

Inasmuch as areo clubs are classified an nonappropriated fund activities, commercial public liability insurance is not required. However, where it is determined that local circumstances make it advisable, such coverage may be obtained when specifically approved by the Air Force Welfare Board. Requests for exception should be submitted through channels to Headquarters USAF, ATTN: AFPMP-WB. All civilians and foreign nationals rifing as passengers will accomplish a Release From Claim For Injury or Death, outlined in AFR 76-6, prior to flights in aero club aircraft.

BY ORDER OF THE SECRETARY OF THE AIR FORCE:

THOMAS D. WHITE
Chief of Staff

Official:
J. L. TARR
Colonel, USAF
Director of Administrative
Services

2. The Constitution of the Castle Air Force Base Aero Club provided:

C O N S T I T U T I O N

ARTICLE I
Name

The name of this Organization shall be the CASTLE AIR FORCE BASE AERO CLUB.

ARTICLE II
Purpose

The purpose of this Organization shall be to stimulate an interest in aviation; to provide authorized personnel with an opportunity to engage in flying as a recreational activity; and to encourage and develop skills in aeronautics, navigation, mechanics and related aero-sciences useful to the Air Force mission.

ARTICLE III

Section A. Membership shall be on a voluntary basis and open to active-duty personnel and their dependents, retired military personnel and their dependents, and civilians employed by the Air Force who are paid from appropriated or nonappropriated funds.

Section B. The number of members shall be limited at the discretion of the Executive Board, based on the amount of equipment available so as to afford each active member an opportunity to fly a reasonable amount of time and engage wholeheartedly in all phases of club activities.

Section C. A member may be suspended indefinitely or for a stated period by majority vote of the Executive Board in the event that:

1. The conduct of the member is prejudicial to the best interests of the club.

2. The member fails to discharge his indebtedness to the club.

Section D. Membership shall be terminated upon written notification to the Secretary by the individual concerned, or, for cause, by majority vote of members of the Executive Board.

ARTICLE IV

Executive Board

The Officers of this Organization shall be the President Vice-President, Secretary, Treasurer, Operations Manager, and Aircraft Maintenance Director. These officers shall comprise the Air Force Aero Club Executive Board, and all matters of policy shall be handled through this group for approval by a majority of the club members.

ARTICLE V

Finances

It is the responsibility of the Executive Board to insure that the club operates on a self-supporting basis in a business-like manner to assure financial stability at all times. Initiation fees, membership dues, rental fees and other financial assessments shall be determined by the Executive Board.

ARTICLE VI

Liability

Insurance shall be carried on all aircraft to protect the members from liability and damages incurred while participating in bona fide club activities. No member can obligate the Aero Club except as set forth in the Constitution and By-Laws.

ARTICLE VII

Quorums and Meetings

Section A. The time, place, and frequency of general meetings shall be determined by the Executive Board. One-third of the total membership will constitute a quorum.

Section B. The President of the Executive Board shall determine the time, place and frequency of Executive Board meetings. Three members shall constitute a quorum.

ARTICLE VIII

Amendments

This Constitution may be changed, amended or superseded only by a two-thirds vote of the membership at a general meeting. At least seven days in advance, the membership must

be notified of matters to be considered at meetings during which any proposed change, amendment, or supersession of this Constitution is to be considered.

ARTICLE IX

Dissolution

Upon dissolution of the Aero Club the Executive Board shall be designated as a Board of Trustees to liquidate the assets of the club as soon as possible and to pay all existing debts and liabilities in proportion to the final available capital, including any money due to members as refunds. The disposition of residual assets will be as prescribed by applicable Air Force Regulations.

2. The By-Laws of the Castle Air Force Aero Club provided in pertinent part:

BY-LAWS

1. PURPOSE. The purpose of this Air Force Aero Club shall be to stimulate an interest in aviation and provide personnel with an opportunity to engage in recreational flying and to encourage and develope skills in aeronautics, navigation, mechanics and related aero-sciences useful to the Air Force mission.

* * * * *

3. EXECUTIVE BOARD.

a. The powers, business and property of the Club shall be exercised, conducted and controlled by the Executive Board of six (6) members.

b. Each member of the Executive Board shall be elected at the annual meeting of the members of the Club.

c. In case of a vacancy on the Board, the remaining Board members shall fill such vacancy by appointment from the Club membership. If three or more vacancies occur at any one time, they shall be filled by vote of the members at the meeting duly called.

d. Immediately after each annual meeting of members, the newly elected Board members shall hold a meeting and organize by election of President, Vice-President, Secretary,

Treasurer, Operations Manager and Aircraft Maintenance Director shall be elected by the Executive Board from their own number at the first meeting after organization of the Club and thereafter at the first meeting after the regular annual meeting of the members. They shall hold office for one year and until their successors are elected and qualified.

e. The President and Vice-President shall serve without compensation or reward. The Secretary, Treasurer, Operations Manager, and Aircraft Maintenance Director may each receive a specified amount of flying time per month as compensation for their services.

f. The Treasurer shall be bonded, the premium therefor to be at the expense of the Club.

4. PRESIDENT.

A. The President shall be the chief executive of the Club. He shall preside at all meetings of the Club and the Executive Board. He may call any special meeting of the members of the Executive Board and shall have, subject to the advice and control of the Board members, general charge of the business of the Club. He shall execute with the Secretary, in the name of the Club, all certificates of membership, contracts, and instruments other than checks following their approval by the Executive Board.

b. The President shall be responsible to the Executive Board for the operation of the Club. He shall make and enforce decisions regarding the suitability of all equipment and the qualifications of all members for every type of flight operation. He shall recommend for approval to the Executive Board all operational rules of the Club. He shall report all violations of those rules by any member and make recommendations to eliminate such violations.

* * * * *

13. MEMBERSHIP.

a. New members may be admitted to the Club only after being approved by a unanimous vote of the members. Membership shall be limited in number for the first aircraft, with not more than a total of 25 for any additional aircraft.

b. A person duly elected to this Club shall be deemed a member upon payment of an initiation fee. Each member shall be assessed monthly dues in the amount prescribed by the Executive Board, for a period of 12 months, said dues to be payable one month in advance, due on the 15th day of each month. The monthly dues shall be reduced at the end of the 12 month period at the discretion of the Executive Board.

c. Upon receipt of the initiation fee, the Club shall issue to each member a certificate of membership on a form approved by the Executive Board.

d. A member may withdraw from the Club upon written notification to the Secretary 30 days in advance, and said member may make his withdrawal final within the next 90 days without furthur (sic) notification, provided that the withdrawing member has disposed of his share in the assets of the Club to the Club or to a new member acceptable to the Club. The Club shall have the first option to purchase the share of a member wishing to withdraw from the Club and the Club shall have 30 days from the withdrawal notice to exercise this option.

c. Any member who has failed to pay his dues or any sum due the Club within 15 days after said sums shall be due, shall be considered a delinquent member and shall be automatically suspended from flying the Club aircraft. Wheb (sic) a deliquent member fails to pay his dues, to pay any sum owed to the Club or to make appropriate arrangements with the Executive Board for the payment thereof within 60 days of the due date, the member shall automatically be considered as indicating his intention to withdraw.

f. A member may be expelled by a two-thirds vote of the members voting at any regular or special meeting. Ten days notice shall be given to each member, who shall have the right to be heard either in person or by counsel at a meeting of the Club for this purpose. A member so expelled shall receive from the Club a sum equal to his original membership fees less any dues or other monys owed to the Club.

No. 18831

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

In the Matter of

ALEXANDER T. CHOHON,

Bankrupt.

OPENING BRIEF OF APPELLANTS.

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TOPICAL INDEX

TABLE OF AUTHORITIES CITED

No. 18831

IN THE

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In the Matter of

ALEXANDER T. CHOHON,

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OPENING BRIEF OF APPELLANTS.

Introductory Statement.

This appeal is prosecuted by C. Douglas Wikle, Trustee in Bankruptcy of the above entitled estate, and involves the validity of a joint declaration of homestead of the bankrupt and his wife upon the joint tenancy interest of the bankrupt in the home of himself and wife, Agnes D. Chohon, held in joint tenancy, and which declaration of homestead was not recorded until one year, seven months and eighteen days after the filing of the bankruptcy herein.

Jurisdictional Statement.

The Court has jurisdiction of this appeal pursuant to the provisions of Section 24a of the Bankruptcy Act.

Statement of the Case.

There was an involuntary petition in bankruptcy filed herein on February 18, 1959, and the adjudication was entered therein on the 15 day of March, 1960.

C. Douglas Wikle was appointed trustee of the estate on the 13 day of December, 1960, and duly qualified by the filing of his bond in the sum of $10,000.00 on December 15, 1960.

The trustee filed his report of exempt property on August 1, 1961 refusing to set the homestead aside as exempt; that objections by the bankrupt to the trustee's determination of exempt property was filed herein on August 9, 1961.

The joint declaration of homestead of the bankrupt, Alexander D. Chohon was recorded on October 6, 1960. No declaration of homestead had theretofore been recorded.

On November 29 and 30, 1956, for a valuable consideration consisting of a loan in the sum of Forty Five Thousand and no/100 ($45,000.00) Dollars from Title Insurance and Trust Company, Alexander T. Chohon and his wife Agnes D. Chohon signed and delivered a grant deed to Title Insurance and Trust Company to that certain real property described as Lots 179, 180, 181, 182 and 183 of Tract No. 7101, County of Los Angeles, State of California as per map recorded in Book 77, Pages 32 and 33 of Maps in the office of the County Recorder of said county, and hereinafter described as the home property, to Title Insurance and Trust Company. Although in the form of grant deeds absolute on their face, the said conveyance was in fact a security transaction, reserving to Bankrupt and his wife equitable title to said real property pursuant to a Declaration of Trust executed on November 29, 1956, and recorded on August 8, 1960, by Title Insurance and Trust Company.

Question Presented.

The main question presented by this appeal involves the validity of a declaration of homestead of the Bankrupt under the laws of the State of California and the Bankruptcy Act, where the declaration of homestead was not recorded until more than one and one half years subsequent to the filing of the involuntary petition in bankruptcy against the Bankrupt.

The Laws of the State of California Govern in the Determination of the Validity of the Homestead.

The provisions of the Civil Code beginning with Section 1237 to Section 1304 inclusive, prescribes the procedure and manner of selecting a homestead and of abandoning same, and the law generally in relation to homesteads.

Sections 1262, 1263 and 1264 Civil Code, provide the necessary steps to be taken in order to perfect a valid homestead, one of which is the necessity for the recordation of same in the county in which the land is situated. See Section 1264, Civil Code.

Section 1241 Subdivision 1 provides:

> "The homestead is subject to execution *or* forced sale in satisfaction of judgments obtained;
>
> 1. Before the declaration of homestead is recorded, and which, at the time of such recordation, constitute liens upon the premises. . . ." (Emphasis ours.)

This clearly shows that under the laws of California a homestead is subject to either the levy of an execution or to a forced sale in satisfaction of judgments obtained, if either preceded the recording of the declaration of homestead.

Section 542 C. C. P. provides for the manner in which property may be attached, and Section 688, C. C. P., in defining what property is liable to execution, says:

> "All goods, chattels, moneys or other property, both real and personal, or any interest therein, of the judgment debtor, not exempt by law, except one-half of the earnings of the defendant or judgment debtor received for his personal services rendered at any time within 30 days next preceding the levy of attachment or execution, and all property and rights of property seized and held under attachment in the action, are liable to execution."

Bankruptcy Act Provisions.

Section 6 of the Bankruptcy Act provides for the allowance of exemptions which are prescribed by the laws of the United States or by the State laws in force at the time of the filing of the petition in the State wherein the bankrupt has his domicile for six months preceding the filing of the petition.

Sections 70a and 70e of the Bankruptcy Act are pertinent to the issues here involved.

Section 70a of the Bankruptcy Act provides in part:

> "The trustee of the estate of a bankrupt and his successor or successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this Act, except insofar as it is to property which is held to be exempt, to all of the following kinds of property wherever located. . . ."

and among the property described under sub-paragraph (5) of Section 70a of the Bankruptcy Act is:

> ". . . property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered: Provided . . ."

Nature of Bankrupt's Interest in Property Attempted to Be Homesteaded.

Without question the interest of the Bankrupt in the home property on February 18, 1959, was such an interest which could have been transferred by the bankrupt within the meaning of Subdivision (5) of Section 70a of the Bankrupt Act or which could have been levied upon under Section 688 of C. C. P.

The Bankrupt's Interest in the Home Property Passed to the Trustee of the Bankrupt's Estate on February 18, 1959 at the Moment the Involuntary Petition in Bankruptcy Was Filed.

The filing of the petition in bankruptcy was February 18, 1959. On that date, and at the moment the bankruptcy petition was filed, the trustee herein, upon his appointment and qualification, was vested under Section 70a of the Bankruptcy Act, by operation of law, with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this Act.

If the bankrupt's interest in this home was property described in Section 70a of the Bankruptcy Act, then it became vested in C. Douglas Wikle when he became the qualified Trustee herein, not on the day that he qualified, but as of February 18, 1959.

Certainly an equitable interest in a home is an interest in land which the bankrupt could have, prior to February 18, 1959, transferred within the meaning of Section 70a(5). Therefore, it was property which reverted to C. Douglas Wikle, the Trustee, as of February 18, 1959, although his appointment as Trustee came much later.

It is wholly unnecessary for the Trustee to resort to Section 70c to defend his position here, and the fact that the provisions of Section 70a were not discussed by the Court in *Sampsell v. Straub,* 194 F. 2d 228, is no indication that it is inapplicable to the facts herein. Indeed, we submit it is controlling. The courts have held time and again that the line of demarcation in bankruptcy is the time of the filing of the petition.

How could the bankrupt possibly acquire a homestead upon an interest in property which had months before passed to his trustee in bankruptcy?

While Section 70a excepts property "which is held to be exempt" from passing to the trustee, a homestead exemption under the California law is not exempt and cannot be held to be exempt unless and until the person claiming the homestead prepares, executes and records the declaration of homestead in the manner provided by California law.

A home in California may be the proper subject for a homestead, but if the owner thereof fails to perfect the declaration of homestead and record the same as provided by California law prior to bankruptcy, then a late recordation will avail him nothing.

In *White v. Stump,* 266 U. S. 301, 45 S. Ct. 103, the Supreme Court was passing upon the validity of

a homestead exemption which arose under the laws of the state of Idaho, whose homestead laws appear to be very similar to California. In other words the laws of the State of Idaho require that in order to acquire a valid homestead exemption there must be a declaration made that the land is both occupied and claimed as a homestead and must be recorded: It must be executed and acknowledged like a conveyance of real property and must be filed for record in the office of the County Recorder.

The Court says:

> "The exemption arises when the declaration is filed, and not before. Up to that time, the land is subject to execution and attachment like other land; and where a levy is effected while the land is in that condition the subsequent making and filing of a declaration neither avoids the levy nor prevents a sale under it."

The Supreme Court, after commenting upon a decision arising in this Court (*Brandt v. Mayhew,* 218 Fed. 422) with which it apparently did not agree, and after citing cases which held to the view that under the Bankruptcy Act the right to such an exemption must be tested by the situation existing when the petition in bankruptcy is filed, and held that where the land is not then exempt under the State law it passes to the Trustee for the benefit of the creditors, it goes on to say:

> "These and other provisions of the Bankruptcy Law show that the point of time which is to separate the old situation from the new in the bankrupt's affairs is the date when the petition is

filed. This has been recognized in our decisions. Thus we have said that the law discloses a purpose 'to fix the line of cleavage' with special regard to the conditions existing when the petition is filed (*Everett v. Judson,* 228 U. S. 474, 479, 32 S.Ct. 568, 57 L. Ed. 927, 46 L.R.A. (N.S.) 154), and that 'it is then that the bankruptcy proceeding is initiated, that the hands of the bankrupt and of his creditors are stayed and that his estate passes actually or potentially into the control of the bankruptcy court' (*Bailey v. Baker Ice Machine Co.,* 239 U. S. 268, 275, 36 S. Ct. 50, 54, 60 L.Ed. 275; *Acme Harvester Co. v. Beekman Lumber Co.,* 222 U. S. 300, 307, 32 S. Ct. 96, 56 L.Ed. 208). When the law speaks of property which is exempt and of rights to exemptions, it of course refers to some point of time. In our opinion this point of time is the one as of which the general estate passes out of the bankrupt's control, and with respect to which the status and rights of the bankrupt, the creditors and the trustee in other particulars are fixed. The provisions before cited show—some expressly and other impliedly—that one common point of time is intended and that it is the date of the filing of the petition. The bankrupt's right to control and dispose of the estate terminates as of that time, save only as to 'property which is exempt.' Section 70a. The exception, as its words and the context show, is not of property which would or might be exempt if some condition not performed were performed, but of property to which there is under the state law a present right of exemption—one which with-

draws the property from levy and sale under judicial process.

"The land in question here was not in that situation when the petition was filed. It was not then exempt under the state law, but was subject to levy and sale. One of the conditions on which it might have been rendered exempt had not been performed. Under the state law the fact that the other conditions were present did not suffice. The concurring presence of all was necessary to create a homestead exemption."

It will be noticed that the facts in the *White v. Stump* case are very similar to the facts here, and that the case was decided under the Idaho law which, in effect, is the same as the law of California under which this case must be decided.

It will also be noticed that the Supreme Court decided the *White* case upon the strength of the provisions of Section 70a of the Bankruptcy Act without mention of the provisions of Section 70c of the Act. For the same reasons as prevailed in the *White v. Stump* case, the decision in this case can be determined without the aid of Section 70c of the Bankruptcy Act.

The case of *Myers v. Matley,* 318 U. S. 622, 63 S. Ct. 780 is not in point here for the reason that it is based upon the law of the State of Nevada which permits the filing of a homestead even after a levy of execution and before sale. The Supreme Court in *Myers v. Matley,* 318 U. S. 622, 63 S. Ct. 780, distinguishes between the law of Nevada and Idaho, and says:

"If the law of Nevada respecting homestead exemptions were like that of Idaho, *or operated in*

the same way, White v. Stump would be in point." (Emphasis ours.)

See 145 A. L. R. 503 where the cases of *White v. Stump* and *Myers v. Matley* are distinguished.

Exemptions are ordinarily determined as of the date of filing bankruptcy.

9 Am. Jur. 2d, pp. 493-494, Paras. 652-653.

Sec. 6, Bankruptcy Act, and

Sec. 70a, Bankruptcy Act, which vests the trustee in bankruptcy with the title of the bank as of that date.

See also 25 Cal. Jur. 2d, page 433, paragraph 116, which is to the same effect.

See also 9 Am. Jur. 2d, 494, Par. 653 upon the necessity for perfecting homestead prior to bankruptcy.

The Provisions of Section 70c of the Bankruptcy Act Are Not in Conflict With the Above Cited Law, nor Do the Provisions Thereof Support the Contention of the Bankrupt Which Were Presented to the District Court Upon Review.

Section 70c of the Bankruptcy Act provides in part as follows:

> ". . . The trustee, as to all property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt could have obtained a lien by legal or equitable proceedings at the date of bankruptcy, shall be deemed vested as of such date with all the rights, remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such a creditor actually exists."

Under this section the trustee is vested as of the date of bankruptcy "with all the rights, remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such creditor actually exists." And this refers to a lien which could have been obtained by legal or equitable proceedings at the date of bankruptcy.

One of such liens would be a lien by virtue of a writ of execution served by the Sheriff upon a piece of real property. Under Section 688 C. C. P., such a lien would be valid against the bankrupt's interest regardless of whether his interest therein was an equitable interest or otherwise.

The case of *Belieu v. Power,* 54 Cal. App. 244, cited by the District Judge in his opinion, at pages 246, 247, distinguishes between a judgment lien and an execution lien and says at page 246:

> "The judgment was docketed before, and the homestead declaration was filed after the date of the contract of purchase. It becomes necessary, therefore, to inquire whether the inchoate right acquired by the respondent under his contract of purchase constituted such ownership of real property as rendered it subject to the lien of the judgment. It is clear, and is perhaps conceded, that property must be 'owned' by the judgment debtor before any lien can attach. It is not, by any means, every interest in property to which the lien of a judgment will attach, nor will it, in fact, attach to every species of property. The lien is not even a uniform consequence of the fact that a contract lien upon the property may be protected by the recording laws, as in the case of various classes of personal property; nor that the property

> may be taken under execution issued upon the judgment, as is seen in the case of personal property of every class. The whole matter is statutory. If it were purely a question of logic, it might be inquired why, if the lien of a chattel mortgage is, under certain conditions, protected by the recording laws, the lien of a judgment against the same classes of property should not, in like manner, be protected. Or, if certain inchoate interests in real property *may be seized on execution,* why they should not be subject to a judgment lien."

and then goes on to say:

> "Property interests of any and every kind, whether real or personal, and every interest therein are subject to seizure under attachment or levy on execution, unless exempt from execution. (Secs. 542 and 688, Code Civ. Proc.) While many classes of property may be taken on execution, only two classes are subject to the lien of a judgment—real property owned by the debtor at the time of docketing and real property that he may afterward acquire. While any interest in real property, legal or equitable, may be seized and sold under execution, only real property actually owned by the judgment debtor will support a judgment lien."

If a lien which a creditor could have obtained by legal or equitable proceedings at the date of bankruptcy is the test of the trustee power, "whether or not such creditor actually exists" then certainly he is in the position of an execution creditor who has levied upon an interest in real property and he is not confined to the position of a creditor holding a recorded abstract of judgment.

There are various kinds of liens in addition to a recorded abstract of judgment which are included in the definition of Section 70c of the Bankruptcy Act.

It will bear repeating that property held pursuant to an execution lien has priority over a subsequently recorded declaration of homestead. Section 688 C. C.

We respectfully submit that the judgment of the United States District Court herein should be reversed, and that the homestead of the bankrupt herein should be held to be invalid against the trustee's interest in the property in question.

Respectfully submitted,

UTLEY & HOUCK,
By ERNEST R. UTLEY,
Attorneys for Trustee.

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

ERNEST R. UTLEY

No. 18831

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

In the Matter of

ALEXANDER T. CHOHON,

Bankrupt.

APPELLEE'S BRIEF.

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In the Matter of

ALEXANDER T. CHOHON,

Bankrupt.

APPELLEE'S BRIEF.

Statement of the Case.

Appellee, bankrupt herein, concurs in the Statement of the Case presented by appellant in his opening brief, but desires to add the following two facts thereto: The grant deeds referred to dated November 29 and November 30, 1956, were recorded on the dates which they bore, and thereafter legal title to the home property has remained and still remains vested in Title Insurance and Trust Company. On December 22, 1960, in the Schedules filed by bankrupt, he claimed a homestead exemption on the home property.

Summary of Argument.

1. Section 70a of the Bankruptcy Act vests the trustee with title only to bankrupt's non-exempt property, and is not determinative of the time and manner of claiming such exemptions.

2. In order to ascertain whether property is exempt, analysis must be made of the applicable State laws dealing with exemptions.

3. Appellee's declaration of homestead which, in the absence of bankruptcy, would have prevailed in California against any lien creditor at the time of its filing, will prevail against the trustee.

1. **Section 70a of the Bankruptcy Act Vests the Trustee With Title Only to Bankrupt's Non-Exempt Property, and Is Not Determinative of the Time and Manner of Claiming Such Exemptions.**

Section 70a of the Bankruptcy Act (11 U. S. C. § 110) provides in part as follows:

> "The trustee of the estate of a bankrupt . . . upon his . . . appointment and qualification shall in turn be vested by operation of law with the title of the bankrupt as of the date of filing of the petition initiating a proceeding under this act *except insofar as it is to property which is held to be exempt* . . . (Emphasis added.)

The trustee contends that Section 70a is controlling herein, asking "how could the bankrupt possibly acquire a homestead upon an interest in property which had months before passed to his trustee in bankruptcy?" (A. O. B. p. 6.) He argues, in essence, that under Section 70a, he became vested with all of the property of the bankrupt as of the date of the filing

of the petition in bankruptcy, and the bankrupt could not thereafter claim an exemption in the home property. This cannot be a correct statement of the law, as a simple illustration will show:

California Code of Civil Procedure Sections 690.1-690.25, inclusive, afford to claimants thereof a number of exemptions, frequently calling for selection of certain items from among a class of similar items. If the trustee's argument were correct, it would be impossible for any bankrupt against whom an involuntary petition has been filed to make the necessary claim and selection provided by those sections, since the trustee would have become vested with the bankrupt's interest in all the properties of the bankrupt, whether or not described therein, and all claims of exemption, which are not made until the bankrupt files his Schedule, would be cut off.

This is not the meaning of Section 70a. That section applies only to non-exempt property, and does not deal with the time or manner of claiming exemptions.

Brandt v. Mayhew, 218 Fed. 422 (1914).

Under the 1938 Amendment to Section 70a (changing from "except insofar as it is to property which is exempt," to "property which is held to be exempt") "a homestead is exempt if, under the State law, it would be held to be exempt."

Myers v. Matley, 318 U. S. 622, 63 S. Ct. 780 (1943).

2. In Order to Ascertain Whether Property Is Exempt, Analysis Must Be Made of the Applicable State Laws Dealing With Exemptions.

In support of his position, appellee herein will cite three landmark cases in the area of homestead exemptions, *White v. Stump,* 266 U. S. 310, 45 S. Ct. 103 (1924), *Myers v. Matley, supra,* and *Sampsel v. Straub,* 194 F. 2d 288 (9th Cir. 1952) *cert. denied* 343 U. S. 927, 72 S. Ct. 76 (1952). In each of these cases, a homestead declaration was filed after the filing of a petition in bankruptcy, and in each such case, an analysis was had of the State law pertaining to homesteads and creditors' rights in order for each of the courts involved to make its judgment. It is respectfully submitted that if the trustee were correct in his position that Section 70a answers all questions herein, none of these cases would have any meaning or significance. However, a detailed analysis of these three cases will indicate to the court the necessity of analyzing California law in order to ascertain whether the homestead herein filed is valid against the trustee.

In *White v. Stump, supra,* a voluntary bankruptcy was filed, and one month later, a homestead declaration recorded in accordance with Idaho law. Under the then existing law in Idaho, in the absence of bankruptcy, any creditor who had levied under an attachment or execution would prevail over a subsequently filed homestead. The court held that the exemption in Section 70a "is not of property which would or might be exempt if some condition not performed were performed, but of property to which there is under state law a present right of exemption—one which would withdraw the property from levy and sale under ju-

dicial process." (266 U. S. at 313.) Hence, in that case, since the bankrupt's creditors could have reached the land by levy and sale, the court held the property not to be exempt.

In *Myers v. Matley, supra,* the court initially distinguished the *White v. Stump* case, since under Nevada law, applicable in the *Myers* case, a homestead declaration would protect the land even after a levy had been made by a creditor, if the declaration was recorded at any time before sale.

The court stated that

> "historically, and under the theory of the present Act, bankruptcy has the force and effect of the levy of an execution for the benefit of creditors to insure an equitable distribution among them of the bankrupt's assets. The trustee is vested not only with the title of the bankrupt, but clothed with the right of an execution creditor with a levy on the property which passes into the trustee's custody."

Appellee herein urges the significance of the foregoing language upon the court, in that it becomes obvious therefrom that the status of the trustee under Section 70a and 70c is as one who takes the bankrupt's title to non-exempt property. But as to property as to which a claim of exemption is made, in determining that claim of exemption, the trustee stands in the shoes of a lien creditor. If that lien creditor has no rights under applicable state law, then neither does the trustee as to the property in question, and the property is exempt.

The Court in the *Myers* case, reaching this conclusion, held that

> "in conformity to the principle announced in *White v. Stump,* that the bankrupt's right to a homestead exemption becomes fixed at the date of the filing of the petition in bankruptcy, and cannot thereafter be enlarged or altered by anything the bankrupt may do, it remains true that, under the law of Nevada, the right to make and record the necessary declaration of homestead existed in the bankrupt at the date of filing the petition, as it would have existed in case the levy had been made upon the property. The assertion of that right before actual sale in accordance with state law did not change the relative status of the claimant and the trustee subsequent to the filing of the Petition." (318 U. S. at 628.)

In *Sampsel v. Straub, supra,* the lower courts had recognized that Section 70a was inadequate to solve the problem where the bankrupt had filed a declaration of homestead subsequent to the filing of the petition in bankruptcy. This court was required to analyze Section 70c of the Bankruptcy Act, and it is on that analysis that the *Sampsel* decision stands.

Section 70c of the Bankruptcy Act provides in part as follows:

> ". . . the trustee, as to all property . . . upon which a creditor of the bankrupt could have obtained a lien by legal or equitable proceedings at the date of bankruptcy, shall be deemed vested as of such date with all of the rights, remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such a creditor actually exists."

The *Sampsel* case turned on an analysis of California law, and the California cases which stand for the rule that a judgment creditor with abstract of judgment recorded is entitled to a lien upon all non-exempt real property to which the judgment debtor has *legal* title.

From the foregoing cases, the following general rules emerge:

Section 70a of the Bankruptcy Act does not determine in and of itself that if the bankrupt owns an interest in real property as of the date of the filing of the petition, and subsequently records a homestead thereon, every such homestead declaration is invalid.

A homestead recorded after the filing of a petition in bankruptcy will be valid and the trustee must recognize the exemption, if, under state law, a lien creditor's rights could be defeated by the filing of the homestead. That is to say, if the homestead declaration will defeat the rights of a judgment-creditor it will defeat the rights of the trustee.

3. Appellee's Declaration of Homestead Which, in the Absence of Bankruptcy, Would Have Prevailed in California Against Any Lien Creditor at the Time of Its Filing, Will Prevail Against the Trustee.

Bankrupt herein, it will be recalled, as of the date of the filing of the petition in bankruptcy, had only an *equitable* title to the real property involved, and did not have legal title. Legal title rested in Title Insurance and Trust Company.

California Code of Civil Procedure, Section 674 allows a judgment creditor to record an abstract of his judgment, which becomes a lien on the real property of the judgment debtor. However, such a judgment credi-

tor is entitled to a lien only upon real property to which the judgment debtor holds legal title. Where the judgment debtor has merely equitable title, no lien is created thereon by the recordation of an abstract of judgment.

Merchantile Collection Bureau v. Roach, 195 Cal. App. 2d 355, 15 Cal. Rptr. 710 (1961);

Homeland Building Co. v. Reynolds, 49 Cal. App. 2d 176, 121 P. 2d 59 (1942).

In *Poindexter v. Los Angeles Stone Co.,* 60 Cal. App. 686, 214 Pac. 241 (1923), a judgment creditor attempted to assert a lien of judgment against the interest of a beneficiary of a trust in real property. The court held that the lien of the judgment attaches to legal interests only, and not to equitable interests. This was true although the legal interest involved was mere formal title, the full beneficial interest being in the judgment debtor.

Thus, a California judgment creditor, with abstract of judgment recorded has a lien only upon real property wherein the judgment debtor has legal title, and his lien does not reach property to which the debtor has only equitable title. On the other hand, a declaration of homestead may be filed by a person regardless of whether he has legal or equitable interests in the real property. *Alexander v. Jackson,* 92 Cal. 514, 28 Pac. 593 (1891) holds that an equitable title is sufficient to support a homestead declaration.

Thus, where an equitable interest in real property is all that is held by the bankrupt, California law dealing with homestead declarations is exactly the same as Nevada law concerning all homestead declarations, and the decision in *Myers v. Matley,* should be controlling. Under Nevada law, as set forth in *Myers,* a declaration

of homestead filed at any time before sale will defeat the rights of a lien creditor. In California, where equitable title is all that is held, a declaration of homestead recorded before execution sale, will defeat the rights of any creditor.

The trustee attempts to avoid this result, by asserting that "property held pursuant to an execution lien has priority over a subsequently recorded declaration of homestead." (A. O. B. p. 13.) The trustee's assertion is without authority, and does not represent the law in California. In California, there is but one way of constituting a judgment a lien on the debtor's land, and that is the filing of an abstract thereof, in the Office of the Recorder of the County in which the land is situated. The lien of an execution or an attachment does not have this effect. The court so held in *Beaton, et al. v. Reid, et al.,* 11 Cal. 484, 44 Pac. 167 (1896), wherein a judgment creditor had a writ of execution issued and levy made by the Sheriff upon the premises in dispute, and notice of sale under said execution given. Subsequent to the levy, but before the sale, the judgment debtor declared a homestead on the premises, and then brought an action to enjoin the sale. No abstract of judgment had been recorded, and the court stated that

> "the levy of the execution in question did not have the effect to prevent the premises from being impressed with the homestead character at any time before the sale; and that, the lien of the execution not being one of those specified in the Civil Code for which the homestead can be taken, the judgment of the court below enjoining the sale and the execution of the deed thereunder was right."

See also:

Yager v. Yager, 7 Cal. 2d 213, 60 P. 2d 422 (1936).

Summary and Conclusion.

From the foregoing, it becomes clear that the real test of whether or not property is exempt under Section 70a is the following: Had there been no bankruptcy filed, and a homestead declaration recorded, on the date on which said declaration was recorded, could there have been a creditor whose lien would prevail? In *White v. Stump, supra,* any creditor who had previously levied on the real property would have prevailed over the homestead declaration and so the exemption was denied. In *Sampsel v. Straub, supra,* where the bankrupt held legal title to the property, a creditor who had recorded his abstract of judgment would have prevailed. But in *Myers v. Matley, supra,* no creditor would have prevailed, as the homestead declaration took precedence over any prior levy, unless it went all the way to sale, and in that case, the homestead exemption was granted.

Applying that test to the instant case, in California no judgment creditor with an abstract of judgment recorded could have prevailed over a subsequently recorded homestead. The judgment creditor, with abstract recorded, has a lien only on real property to which the debtor holds legal title; where the debtor holds equitable title, the lien is ineffective. When appellee and his wife recorded their declaration of homestead, there were no creditors whose liens could have prevailed over that homestead declaration had there been no bankruptcy. The trustee takes no greater right to reach

exempt property than creditors under the laws of California. If those creditors had no lien on the property and the bankrupt claims an exemption thereon, the trustee has no rights therein.

It is therefore respectfully submitted that the judgment of the United States District Court herein should be affirmed, and that the homestead of appellee herein should be held to be valid and the property exempt.

Respectfully submitted,

SHULMAN AND SHULMAN,
By ADLEY M. SHULMAN,
Attorneys for Bankrupt-Appellee.

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the 9th Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

ADLEY M. SHULMAN

No. 18831

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

In the Matter of

ALEXANDER T. CHOHON,

Bankrupt.

ANSWERING BRIEF OF THE TRUSTEE.

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ANSWERING BRIEF OF THE TRUSTEE.

Comment on "Statement of the Case" in Appellee's Brief.

We cannot accept as a true statement of the facts or as a proper conclusion of law that after the two grant deeds were recorded, legal title to the home property has since remained vested in Title Insurance and Trust Company.

The transaction between the bankrupt and Title Insurance and Trust Company was a loan with security given by the execution of two grant deeds and a declaration of trust in the nature of a trust deed. Under the law of California, the bankrupt and his wife retained legal title in the real estate at all times.

ARGUMENT.

We have not argued the question of the exact nature of the bankrupt's title in our opening brief, except to say: That it is our contention that whatever the bankrupt's interest was in the home on the date of bankruptcy, it was such an interest that vested in the Trustee under the provisions of Section 70a(5) of the Bankruptcy Act when bankruptcy was filed.

That the interest of the bankrupt having vested in the Trustee at the time bankruptcy was filed, could not later be impressed with a valid homestead filed by the bankrupt regardless of whether the bankrupt held an equitable or legal interest. This contention is based upon *White v. Stump*, 266 U. S. 310, 45 S. Ct. 103.

Nature of Security Given by the Bankrupt Upon the Property in Question.

A question of law and fact arises as to whether or not the security transaction between the bankrupt and the Title Insurance and Trust Company constitutes a mortgage (See 33 Cal. Jur. 2d beginning at p. 437) or whether it is a deed of trust (See 33 Cal. Jur. 2d, beginning at p. 490), but in either event, where the grantor conveys the property for security purposes only, and retains possession and control of the land, as was done in this case, he also retains actual title to the land.

A GRANT DEED GIVEN TO SECURE A DEBT IS HELD TO BE A MORTGAGE, AND DOES NOT ACTUALLY CONVEY TITLE TO THE LAND.

33 Cal. Jur. 2d, p. 437, Paragraph 21, says in part:

> "It has long been recognized in this state that a deed absolute in form may be shown to have been intended as a mortgage, and, if it was intended as security for the payment of a debt or the performance of any other obligation, it will be held to be a mortgage. This principle, as laid down by the courts, is substantiated by a statute that provides, in effect, that every transfer of an interest in property made only as security for performance of another act is deemed a mortgage."

33 Cal. Jur. 2d, p. 440, Paragraph 24, says:

> "A conveyance of real property, though absolute in form, given as security for the payment of a note and unaccompanied by a change of possession, is in effect only a mortgage, and merely creates a lien in favor of the grantee. It does not actually convey title, *despite recitals to the contrary.* This is so whether the obligation the deed is given to secure is due to the grantee or to another." (Emphasis ours.)

And, see also *33 Cal. Jur. 2d, p. 442, Paragraph 26,* which says in part:

> "A court does not look to the form of an instrument, but to its real character as having been given for the purpose of securing indebtedness. Even where an agreement bears no visible earmarks of a mortgage, if it was actually entered

into for the purpose of security no form of words, however adroit, can estop a party to plead and prove that fact. If the transfer is made as security, *it is in equity a mortgage irrespective of the form in which made, no matter how expressly the parties may agree that it shall not be deemed a mortgage,* or regardless of how strong the language of the deed or any instrument accompanying it may be. *It is a matter of law, not of contract.*" (Emphasis ours.)

In *Stockel v. Elich*, 112 Cal. App. 588 at 592, the Court says:

"It is true that a deed which is absolute on its face, but which is intended merely to secure an indebtedness of the grantor, is a mortgage and does not actually convey title to the land. *(Moisant v. McPhee, supra.)* It is also true that a mortgage is merely a written contract hypothecating specific property and creating a lien for the security of a debt. (§2920, Civ. Code; 17 Cal. Jur. 696, §5) *Pacific Fruit Exchange v. Duke*, 103 Cal. App. 340 [284 Pac. 729].) A mortgage is not necessarily a grant of real property. (*Adler v. Sargent,* 109 Cal. 42, 49 [41 Pac. 799].)"

In *Moisant v. McPhee,* 92 Cal. 76 at 79, the Court says:

"At the trial, both Warren and appellant testified that the deed put in evidence was given only to secure the payment of an indebtedness on account. The deed was therefore a mortgage, and *did not pass the title to the land* which it purported to convey. (*Taylor v. McLain,* 64 Cal. 514; *Healy v. O'Brien,* 66 Cal. 519; *Raynor v. Drew,* 72 Cal. 309." (Emphasis ours.)

In *Anglo-Californian Bank v. Cerf,* 147 Cal. 384 at 388 to 389, the Court says:

"The fact that the defendant Steinhart, a manager of plaintiff corporation, was named as grantee in the deeds instead of the plaintiff itself, in no degree impairs their validity as mortgages in favor of plaintiff. If authority is needed upon this proposition it is to be found in *Banta v. Wise,* 135 Cal. 277 [67 Pac. 129], where the question was squarely presented in the case of a deed absolute on its face purporting to grant certain realty to one who was a member of a partnership. The deed was enforced as a mortgage in favor of the firm, it being shown that it was given as security for an indebtedness due the firm and to secure contemplated advancements by the firm. It was pointed out in the opinion that the general equitable principle applicable in this class of cases applies equally to all cases of deeds made to secure money, whether due or to become due, 'or whether *due to the grantee or another.*' It was said therein, speaking of a deed made to one as security for the debt of another: 'Such a transaction comes equally within the definition given in the code, which is, that a '"mortgage is a contract by which specific property is hypothecated for the performance of an act, without the necessity of a change of possession"' (Civ. Code, §2920), and also within the provision that '"Every transfer of an interest in property, other than in trust, made only as a security for another act, is to be deemed a mortgage,"' etc. (Civ. Code §2924.) The exception made in the section last cited refers only to the express trusts provided for by other provisions of the code (Secs. 852, 857) which, though in some cases difficult in principle to be distinguished, are

held not to be mortgages. . . . But these decisions apply only to cases where, by the terms of the deed, the trustee is authorized to sell and to apply the proceeds in payment of the debt, and not to deeds where there is no power of sale expressed."

See also:

33 Cal. Jur. 2d, p. 445, Par. 30.

"Since the deed to Lee was intended as a mortgage it transferred no interest in the land but created a lien only."

Lee, et al. v. U. S. Fire Ins. Co., et al., 55 Cal. App. 391.

Where Trust Deeds Are Given to Secure an Obligation the Trustor Is Treated as the Holder of the Legal Title.

The above question is covered in Paragraphs 86 to 91, 33 Cal. Jur. 2d, pages 490 to 496, and at page 492, it is said:

"The legal title is conveyed solely for the purpose of security, leaving in the trustor or his successor a legal estate in the property as against all persons except the trustee and those lawfully claiming under him. Otherwise, the trustor or his successor is treated in all respects as the holder of the legal title. The legal estate thus left in the trustor entitles him to possession of the property until his rights have been fully divested by a conveyance made by the trustee in the lawful execution of his trust, and to exercise all the ordinary incidents of ownership in regard to the property, subject always, of course, to the execution of the trust. In fact, the possessory rights of trustors are said to be the same as those of mortgagors."

The case of *King v. Gotz,* 70 Cal. 236, is cited in support of the above quotation from California Jurisprudence. This case incidentally also involves the validity of a homestead. The Court in this case says, at page 240:

> "The defendant Gotz, notwithstanding the execution of the trust deed, had an interest in the property which he could transfer or devise, subject only to the trust. (Civ. Code, §864.)
>
> And the grantee under him would acquire a legal estate in the property, except as against the trustees and those lawfully claiming under them. (Civ. Code, §865.)
>
> It follows from these provisions (which modify section 863 of the same code) that the trustor of an express trust, except as to his trustee and those holding under him, is treated as the holder of the legal title.
>
> The deeds of trust left an interest in Gotz which could have been sold under execution. (*Kennedy v. Nunan,* 52 Cal. 326.)"

and the case of *MacLeod v. Moran,* 153 Cal. 97 at 100, which also involves the validity of a homestead, says:

> "The nature of such an instrument has been extensively discussed by this court, and the sum and substance of such discussion is that while the legal title passes thereunder, and the trustees cannot be held to hold a mere 'lien' on the property, it is practically and substantially only a mortgage with power of sale. (See *Sacramento Bank v. Alcorn,* 121 Cal. 379 383, [53 Pac. 813]; *Tyler v. Currier,* 147 Cal. 31, 36, [81 Pac. 319]; *Weber v. McCleverty,* 149 Cal. 316, 320, [86 Pac. 706].) The legal title is conveyed solely for the purpose of security, leaving in the trustor or his successors a

> legal estate in the property, as against all persons except the trustees and those lawfully claiming under them. (Civ. Code, Secs. 865, 866.) Except as to the trustees and those holding under them, the trustor or his successor is treated by our law as the holder of the legal title. (*King v. Gotz,* 70 Cal. 236, [11 Pac. 656].) The legal estate thus left in the trustor or his successors entitles them to the possession of the property until their rights have been fully divested by a conveyance made by the trustees in the lawful execution of their trust, and entitles them to exercise all the ordinary incidents of ownership in regard to the property, subject always, of course, to the execution of the trust."

In *Bank of Italy v. Bentley,* 217 Cal. 644, Justice Shenk in commenting at length upon the legal status of the trustor's interest, beginning at ¶(7), p. 654 at p. 656, says:

> "The legal title is conveyed solely for the purpose of security, leaving in the trustor or his successor a legal estate in the property, as against all persons except the trustees and those lawfully claiming under them. (Civ. Code, Secs. 865, 866.) Except as to the trustees and those holding under them, the trustor or his successor is treated by our law as the holder of the legal title. (*King v. Gotz,* 70 Cal. 236 [11 Pac. 656].) The legal estate thus left in the trustor or his successors entitles them to the possession of the property until their rights have been fully divested by a conveyance made by the trustees in the lawful execution of their trust, and entitles them to exercise all the ordinary incidents of ownership in regard to the property, subject always, of course, to the execution of the trust."

In the case of *Hagge v. Drew,* 27 Cal. 2d 368 at 376, the Court says:

"It is urged that, assuming title was in defendants at the time of the contract of sale insofar as a conveyance by the owner was concerned, yet the finding of ownership in fee simple is against the evidence for the interest of defendants in the property was subject to the trust deed they had given to the trustee in bankruptcy; that a person who holds property on which there is a trust deed outstanding is not the owner in fee simple and that plaintiffs did not know of the trust deed when the contract of sale was made and were thereby defrauded. The evidence supports the conclusion that no representations were made by defendants or their agents in regard to the existence or lack of existence of a trust deed against the property, that is, nothing was said about the matter except to the extent that the statement in the contract, that defendants were the owners in fee simple, could be considered as such. There existed no fiduciary relation between plaintiffs and defendants. They were dealing at arm's length. For all practical purposes defendants may have been considered, as found by the court, to be the owners in fee simple of the property even though the trust deed was outstanding. 'Every estate of inheritance is a fee, and every such estate, when not defeasible or conditional, is a fee simple or an absolute fee." (Civ. Code, §762.) A fee simple title is one that is inheritable and the holder has the power to transfer. (See *In re Barlow v. Security T. & S. Bank,* 197 Cal. 263, [240 P. 19].) While it is true that in California the title theory is adhered to with respect to trust deeds and the lien theory with regard to mortgages, yet for practical purposes the

> trustor is the owner of the property. (See *Bank of Italy etc. Assn. v. Bentley,* 217 Cal. 644 [20 P. 2d 940].) In the instant case the defendants were the owners of the property having unrestricted power to dispose of it and to pass title to plaintiffs."

In *Estate of Moore,* 135 Cal. App. 2d 122 at 132, the Court says:

> "Though the trust deed has been analogized to a mortgage, especially between debtor and creditor, whenever necessary to avoid harshness in the application of the rule, it still remains true that title does not pass to the buyer but rests in the trustee for the primary benefit of the seller."

The court in *Wright v. Security-First Nat'l Bank,* 35 Cal. App. 2d 264, was considering a case in which the bank held a $60,000.00 mortgage. Also the owner of the land had entered into a trust whereby she had deeded 1100 acres of land in the San Bernardino mountains to A. J. Wheeler, subject to the mortgage. Wheeler owned adjoining land known as the Heath Ranch. In 1924 Mrs. Wright, Wheeler and James M. Oliver entered into an arrangement to combine the above land with other adjoining land for the purpose of developing a resort and land subdivision to be known as Wrightwood. To this end Wright and Wheeler conveyed their land to the bank under a trust agreement, the bank being named as trustee.

The court in this case in discussing the interest of the appellants, at page 272 says:

> "The first question naturally suggested is whether the interest of the appellants, as trustors, in the real property thus conveyed in trust was personal property or whether they retained an interest in real property which could only be divested as

such. While it is well settled that the grantor in an ordinary trust deed given to secure a debt retains an interest in the real property it is also well recognized that a different situation may exist where property is conveyed under certain trust provisions and for other purposes. It has been held that whether such trust property is to be considered as personalty or as an interest in real estate depends upon the intention of the parties and, in various cases, certain things have been held sufficient evidence of an intention to convert an interest in real property into one in personal property."

See also:

Lynch v. Cunningham, 131 Cal. App. 164;
Ogden's Calif. Real Property Law, p. 658.

Also attached in an Appendix No. 1 to this brief, is an extensive quotation from *Scott on Trusts,* Vol. 1, Sec. 9, pages 81-84.

See also appendix No. 2 which covers more in detail *White v. Stump* and *Myers v. Matley.*

"A debt is not a trust and there is not a fiduciary relation between debtor and creditor as such."

Downey v. Humphreys, 102 Cal. App. 2d 323 at 332.

It will be observed that among the cases cited herein in support of the contention that the trustor under a deed of trust retains legal title, are a number of cases involving the right of such a person to a homestead upon such property. It would therefore appear from the above that the bankrupt, at the time of bankruptcy, had something more than an equitable title. He held all of the incidents of title and was the legal owner. He could still hypothecate or sell or assign his interest therein. His interest was an interest upon which a judgment lien would attach.

Section 70a of the Bankruptcy Act, Vests the Trustee With Title to All Property in Said Section Described as of the Date of the Filing of the Petition in Bankruptcy, Upon Which an Exemption Had Not Then and There Been Perfected, if Certain Acts Are Required to Perfect the Exemption Claim.

Counsel argues that Section 70a of the Bankruptcy Act is not determinative of the time and manner of claiming such exemption.

I shall not attempt to answer in my own language this untenable contention of Appellee when the Supreme Court has so aptly spoken upon this subject. For the convenience of the Court, we again quote, in part, from *White v. Stump,* 266 U. S. 301, 45 S. Ct. 103, which is quoted from extensively in our opening brief at Pages 6, 7, 8 and 9. The language which we now quote is found on Pages 8 and 9 of our opening brief. It is:

> "The bankrupt's right to control and dispose of the estate terminates as of that time, save only as to 'property which is exempt.' Section 70a. The exception, as its words and the context show, is not of property which would or might be exempt if some condition not performed were performed, but of property to which there is under the state law a present right of exemption—one which withdraws the property from levy and sale under judicial process.
>
> 'The land in question here was not in that situation when the petition was filed. It was not then exempt under the state law, but was subject to levy and sale. One of the conditions on which it might have been rendered exempt had not been performed. Under the state law the fact that the other conditions were present did not suffice. The concurring presence of all was necessary to create a homestead exemption.' "

No court could make a plainer or more forceful statement of the law upon this point. It is still the law.

The case of *Myers v. Matley,* 318 U. S. 622, 63 S. Ct. 780, is only helpful or in point here under the State law of California and the facts of this case in two respects: That is, where the Court in the *Matley* case says:

> "If the law of Nevada respecting homestead exemptions were like that of Idaho, or operated in the same way, *White v. Stump* would be in point."

and, second, the Court in this case points out that the latest change in the phraseology of Section 70a of the Bankruptcy Act respecting exempt property, which says: ". . . except insofar as it is to property which is held to be exempt." does not alter the principles applicable to the exemption of homestead property in bankruptcy, and that the intent of Congress was merely to clarify the meaning of the Section. This should answer Appellee's contention on Page 2 of his brief.

Since the laws of Idaho and California are very similar, and the law of Nevada is entirely different, the rule the Court here would be required to follow is the reasoning of *White v. Stump.*

In 145 A. L. R., 503-504, it is said:

> "The doctrine of *White v. Stump* (US) supra, is recognized, and constitutes the starting point for discussion, in *Myers v. Matley* (US) (reported herewith) ante, 498.
>
> *White v. Stump* (1924), 266 U.S. 310, 69 L. Ed. 301, 45 S. Ct. 103, 5 Am. Bankr. Rep. (NS) 1, supra, overruled a decision of the Ninth Circuit which sustained a claim to a California homestead based on a declaration filed after bankruptcy. This was *Brandt v. Mayhew* (1914, CCA 9th) 218 F. 422, 33 Am. Bankr. Rep. 845. Under California

law declarations filed after levy are ineffective. *White v. Stump* (US) supra, therefore applies to render ineffective declarations filed in California after bankruptcy."

In this connection, Appellee cites the case of *Brandt v. Mayhew,* which as we have seen, has been overruled by the Supreme Court in *White v. Stump.*

The Trustee Stands in a More Favorable Position Than the Ordinary Lien Creditor of the Bankrupt to Attack the Validity of a Homestead.

The Trustee, by force of law, stands in the position of the most favored or ideal creditor under Sections 70a and 70c of the Bankruptcy Act, whether or not such a creditor actually exists. These sections are often referred to as the "strong-arm clause" and enables the Trustee to bring all of the bankrupt's property *not exempt at the time of the filing of the petition in bankruptcy* into the estate for the benefit of the creditors. See Vol. 4, *Collier on Bankruptcy,* 14th Ed., beginning at p. 926—also p. 943.

Section 70c of the Bankruptcy Act Now Expressly Fixes the Status of the Trustee in Bankruptcy as to the Bankrupt's Property as of "the Date of Bankruptcy".

Vol. 4, *Collier on Bankruptcy,* 14th Ed., p. 1424, says:

> "It is *not* a prerequisite of the trustee's lien under § 70c that some actual creditor must have fastened a lien on the property at issue by legal or equitable process. A few courts construed former § 47a(2) . . . now the strong-arm clause of § 70c . . . so as to require the existence of an actual lien creditor as a condition of the trustee's lien. These cases were, however, overruled by the

> strong weight of better authority, and the Act of 1938 finally put to rest any conflict over the matter by specifically providing that the strong-arm clause should operate 'whether or not such a [lien] creditor actually exists.' This merely confirmed and ratified the prior decisions so holding. The amendments of 1950 and 1952 retained this explicit language. Accordingly, 'the trustee is, himself, in the position of a lien creditor as a matter of law. That is his legal status."

We have cited at page 6 of our opening brief certain sections of California's Civil Code which provide certain necessary steps to be taken in order to perfect a valid homestead. These sections require affirmative acts by the homesteader before the day of reckoning—the day of the filing of the petition in bankruptcy—the day that the estate of the bankrupt on property not then exempt vests in the Trustee in Bankruptcy by operation of law, and as so plainly stated by the Supreme Court in *White v. Stump.* [See above quotation.]

Status of Trustee as a Lien Creditor Under Section 70c of the Bankruptcy Act.

Vol. 4, *Collier on Bankruptcy*, 14th Ed., p. 1410, says:

> "It was said of the percursor of this provision that it conferred upon the trustee 'by force of law' the status of 'the ideal creditor, irreproachable and without notice, armed cap-a-pie with every right and power which is conferred by the law of the state upon its most favored creditor who has acquired a lien by legal or equitable proceedings.' If the description of the trustee's position under former § 70a was apt, it is even more so under the broader language of the amended § 70c."

Change in Law by 1950-1952 Amendments.

By virtue of the amendment of March 18, 1950 the trustee under § 70c now has all the rights, remedies and powers of a creditor holding a lien thereon obtained by legal or equitable proceedings, whether or not such a creditor actually exists. This section formerly read ". . . rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied." The amendments of 1950 and 1952 made further changes. Each amendment was enacted to further strengthen and fortify the position of the Trustee. *Vol. 33, Collier on Bankruptcy,* 14th Ed., pages 1392 and 1396. The 1952 amendment came subsequent to the decision in *Sampsell v. Straub.*

There is thus no basis for continuing to ascribe to the Trustee the rights, remedies and powers of a particular lien creditor, since he is now vested, at the date of bankruptcy "with all the rights, remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such a creditor actually exists."

See:

Vol. 4, *Collier on Bankruptcy,* 14th Ed., pp. 1392, 1396, and 1493-94.

Courts have occasionally failed to note the change effected by the 1950 and 1952 amendments, hence our reference thereto.

See:

Jackson v. Minick (C. A. 9th, 1958), 260 F. 2d 563;

Mayo v. Petty (W.D.La. 1957), 153 F. Supp. 501.

Exceptions to Exemption of Homestead.

Section 1241 of the Civil Code of California provides:

"The homestead is subject to execution or forced sale in satisfaction of judgments obtained:

1. Before the declaration of homestead is recorded, and which, at the time of such recordation, constitute liens upon the premises.

2. On debts secured by mechanics, contractors, subcontractors, artisans, architects, builders, laborers of every class, materialmen's or vendors' liens upon the premises.

3. On debts secured by encumbrances on the premises executed and acknowledged by husband and wife, by a claimant of a married person's separate homestead, or by an unmarried claimant.

4. On debts secured by encumbrances on the premises, executed and recorded before the declaration of homestead was filed for record. [Enacted 1872; Am. Code Amdts. 1873-74, p. 229; Code Amdts. 1880, p. 7; Stats. 1887, p. 81; Stats. 1951, ch. 1109, §1; Stats. 1957, ch. 1317, §1; Stats. 1959, ch. 1805, §2.]"

The Trustee at the date of the filing of bankruptcy herein, under Section 70c of the Bankruptcy Act, stood in the position of each and all of the lien creditors mentioned in *Civil Code 1241,* with an enforceable lien since such a creditor of the bankrupt could have obtained such a lien by legal or equitable proceedings at the date of bankruptcy. Section 70c certainly includes any lien creditor of the bankrupt who could have obtained a lien by legal or equitable proceedings at the date of bankruptcy, whether or not such creditor exists.

There are certain important comments upon the 1950-1952 changes in Section 70c of the Bankruptcy Act which appear in 1962 Collier Pamphlet Edition of the Bankruptcy Act.

Exemptions Under Sections 690.1 to 690.25, California Code of Civil Procedure, Are Exemptions Allowed as a Matter of Right and Do Not Require Affirmative Action on the Part of the Person Entitled Thereto Prior to the Making of His Claim.

While one in bankruptcy is required to make his claim to exemptions in his schedules (see Schedule B-5 as prescribed by the Supreme Court, as amended May 29, 1961, found in 1962 Collier, Pamphlet Edition of the Bankruptcy Act) and in certain circumstances schedules are filed after bankruptcy, the claim to the exemption must be considered as of the date of the filing of the petition in bankruptcy.

Whether the Rights of the Trustee in This Case Are Measured by the Provisions of Section 70a or 70c of the Bankruptcy Act, or Both, Still the Right of Homestead Exemption to the Bankrupt Should Be Denied.

We respectfully urge that the right of the bankrupt to a homestead was terminated as of the date of the filing of the petition in bankruptcy under Section 70a of the Bankruptcy Act and under the decision of *White v. Stump,* since the property in question was an asset of the bankruptcy estate as defined by Section 70a(5).

Under Section 70c, the Trustee stands in the position of the most favored creditor, for the benefit of all creditors, whether or not such creditor actually exists.

We have shown from California cases cited above, that one who gives a grant deed for the purpose of securing a loan is a mortgagor, and where one in connection therewith executes a trust with power of sale and retains possession and control of the property, is in the position of a person executing a deed of trust; that in

either event, such person does not part with, but retains legal title and therefore, a judgment lien would attach to such an interest.

Conclusion.

Since the Trustee is vested with the title of the bankrupt as of the date of bankruptcy under the provisions of Section 70a, and since he stands in the position of the most favored creditor under Section 70c of the Bankruptcy Act, we respectfully submit that the decision of the District Court should be reversed and that the claim of homestead exemption should be denied.

Respectfully submitted,

UTLEY & HOUCK,
By ERNEST R. UTLEY,
Attorneys for Trustee.

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those Rules.

ERNEST R. UTLEY

APPENDIX 1.

Definitions and Distinctions.

§ 9. *Trust and mortgage or pledge or lien.* Although a mortgagee has an interest in property in which the mortgagor also has an interest, he is not trustee of the property for the mortgagor. In the early English law the common-law courts alone dealt with mortgages. A mortgage was created by a conveyance subject to a condition subsequent by which it was provided that if the debt secured thereby were paid when due, the interest of the mortgagee should cease and the property revert to the mortgagor. Under the earlier law, if the debt were paid when due, the legal title to the property reverted to the mortgagor, but if it were not paid when due, the title of the mortgagee became absolute and indefeasible. Subsequently the Court of Chancery gave relief against the forfeiture caused by the failure to pay the debt when due, and recognized in the mortgagor an equity of redemption. The Court of Chancery took the realistic attitude that the beneficial interest was in the mortgagor and that the mortgagee had merely a security interest. Even under this theory of the mortgage relation, where the mortgagee had the legal title to the mortgaged property and the mortgagor had the equitable beneficial interest in it, the mortgagee was not regarded as trustee for the mortgagor. In many states the courts, sometimes as a result of statutes, hold that the mortgagor not merely has an equitable interest but has legal title to the property subject to a legal security interest in the mortgagee. In such states the resemblance of a mortgage to a trust is even more remote than under the orthodox theory of the relation. Trust and mortgage serve different purposes, and

the consequences arising from the two relationships are different.

The interest of a mortgagee is a security interest. He holds this interest for his own benefit and not for the benefit of the mortgagor. A trustee, on the other hand, has an interest in the trust property which he holds for the beneficiaries, and not for his own benefit. A mortgagee cannot be compelled to surrender his interest in the mortgaged property until the debt secured by the mortgage is paid or otherwise discharged. A trustee has no such interest in the trust property as to permit him to prevent the termination of the trust, if there is no other reason for continuing the trust.[1] The trustee, however, has an interest in the trust property as security for his right to compensation and to indemnity for expenses properly incurred by him in the administration of the trust, and cannot be compelled to surrender the trust property on the termination of the trust until he is paid or secured for the amount thus due him.[2]

There is a fiduciary relation between trustee and beneficiary, but not ordinarily between mortgagee and mortgagor.[3] Thus, although it is a breach of

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[1]See § 337.

[2]See § 345.2.

[3]*England:* Dobson v. Land, 8 Hare 216 (1850); Taylor v. Russell, [1892] A.C. 244.
Alabama: Adler v. Van Kirk Land & Construction Co., 114 Ala. 551, 21 So. 490, 62 Am. St. Rep. 133 (1897).
California: De Martin v. Phelan, 115 Cal. 538, 47 Pac. 356, 56 Am. St. Rep. 115 (1897).
Illinois: Guffey v. Washburn, 382 Ill. 376, 46 N.E.(2d) 971 (1943).
Massachusetts: Dennett v. Tilton, 227 Mass. 299, 116 N.E. 403 (1917).
Oklahoma: Crockett v. Root, 194 Okla. 3, 146 P.(2d) 555

trust for a trustee to transfer the trust property to a third person, a mortgagee can properly transfer his interest in the debt and in the security. Although a trustee is under a duty not to delegate the trust, there is no similar personal relationship between mortgagee and mortgagor which prevents the mortgagee from transferring his interest. In *Taylor v. Russell,*[4] Lord Herschell said: "No authority was cited for the proposition that a mortgagee is, subject to his security, a trustee of the legal estate for the mortgagor. The rights of a mortgagor are no doubt well established in a Court of Equity. He may redeem the mortgage, and no dealings with the property by the mortgagee, save a conveyance under the power of sale, can deprive him of this right. But it is quite a different proposition and one which I think is wholly untenable to assert that a mortgagee is trustee for the mortgagor. It is admitted that a mortgagee may create such estates as he pleases, he may convey, by way of sub-mortgage, to whom and in as many parcels as he pleases."

Similarly, although a trustee is not permitted to profit by purchasing an encumbrance upon the trust property,[5] a mortgagee is not under a like disability in

(1944) (citing Restatement of Trusts, § 9, Comment *c*), noted in 15 Okla. B.A.J. 432.

Oregon: See Harper v. Interstate Brewery Co., 168 Ore. 26, 120 P.(2d) 757 (1942) (citing the text).

Rhode Island: Koury v. Sood, 74 R.I. 486, 62 A.(2d) 649 (1948) (citing the text).

Courts of equity, however, go far in protecting the mortgagor from losing his equity of redemption, particularly where the mortgagee has a power of sale. Cambridge Savings Bank v. Cronin, 289 Mass. 379, 382, 194 N.E. 289 (1935). This matter is beyond the scope of this treatise.

[4][1892] A.C. 244, 255.

[5]See § 170.21.

purchasing prior mortgages. In *Dobson v. Land*[6] the court said: "Now, that a mortgagee is in some sense a trustee for the mortgagor, may be admitted; for every person in whom the legal estate is vested, with a beneficial interest for another person, in a sense, is a trustee for that person . . . a trustee can never make a benefit to himself by any dealing with the trust property; but if a second mortgagee should buy in the first mortgage for half its amount, or even obtain an assignment without consideration from the first mortgagee, I can have no doubt he would be entitled to charge the mortgagor with the full amount of the first mortgage in addition to his own."

Although a pledge has sometimes been spoken of as in the nature of a trust,[7] it is not a trust and has not the legal consequences of a trust. The pledgee does not owe to the pledgor the fiduciary duties owing by trustee to beneficiary. Thus it was held in *Willett v. Herrick*[8] that a purchase by the pledgee from the pledgor of the subject matter of the pledge cannot be set aside on the ground that the pledgee did not make full disclosure to the pledgor. In that case the court said: "As pledgees they were required to use good faith in dealing with the property pledged or in conducting a sale, but this did not impose on them the additional duties of a fiduciary in matters unrelated to the pledge. A pledge is not a trust and the defendants were not trustees in the true sense of the term. . . . Even if the contract were a mortgage, the relation of mortgagor and mortgagee is not of a fiduciary character."

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[6]Hare 216, 220 (1850).

[7]Newton v. Fay, 10 Allen 505, 507 (Mass. 1865); Dibert v. D'Arcy, 248 Mo. 617, 154 S.W. 1116 (1912).

[8]258 Mass. 585, 599, 155 N.E. 589 (1927).

Although the debt which is secured by a pledge is paid off without a return of the property to the pledgor, the pledgee does not become trustee for the pledgor. He might perhaps be called a constructive trustee, but the fiduciary element inherent in the express trust is lacking.[9] Accordingly, it has been held that if the pledgor makes no attempt to compel the return of the property for a long period after the payment of the debt, the pledgor is barred from maintaining an action against the pledgee for the return of the property,[10] although it is well settled that under similar circumstances the beneficiary of a trust would not be precluded from maintaining a suit against the trustee.[11]

There may, of course, be a combination of the two relationships; a mortgage may be held in trust. If a trustee of money lends it and takes a mortgage to secure the loan, he is trustee of the mortgage for the beneficiary of the trust, but he is not trustee for the debtor and there is no fiduciary relation between him and the debtor.[12] On the other hand, a mortgage may be made

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[9]Carpenter & Carpenter, Inc. v. Kingham, 56 Wyo. 314, 109 P.(2d) 463, 110 P.(2d) 824 (1941).

[10]Wehrle v. Mercantile National Bank of Salem, 221 Mass. 585, 109 N.E. 367 (1915); Kase v. Burnham, 206 Pa. 330, 55 Atl. 1028 (1903); Sulkin v. First National Bank & Trust Co., 344 Pa. 251, 25 A.(2d) 166, 139 A.L.R. 1331 (1942); Reynolds v. Hennessy, 15 R.I. 215, 2 Atl. 701 (1886).

But see Stebbins v. Clendenin, 136 Ark. 391, 206 S.W. 681 (1918) (absolute deed as mortgage); Green v. Turner, 38 Iowa 112 (1874) (mortgage).

As to the distinction between a trust and a pledge, see also Colantuoni v. Balene, 95 N.J. Eq. 748, 123 Atl. 541 (1924); State v. Channer, 115 Ohio St. 350, 154 N.E. 728 (1926) (pledgee not guilty of embezzlement).

See note, Pledge as a trust as regards statute of limitations, 139 A.L.R. 1333 (1942).

[11]See §§ 219-219.4.

[12]Dennett v. Tilton, 227 Mass. 299, 116 N.E. 403 (1917); Bradford v. King, 18 R.I. 743, 31 Atl. 166 (1894).

to a person as trustee both for the creditor and for the debtor. Thus a trustee under a deed of trust in the nature of a mortgage is a trustee for and in a fiduciary relation to both the creditor and the debtor.[13] A distinction has been taken between the situation in which property is transferred to a trustee to secure a debt of the transferor to a third person where there is a mortgage in trust and the transferor has an equity of redemption, and the situation in which property is transferred to a trustee to use the property or its proceeds to pay debts of the transferor where the transaction is not a security transaction and the transferor has no equity of redemption, although he is entitled to enforce a resulting trust of any surplus which may remain after the payment of the debts.[14]

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[13]*District of Columbia:* W. A. H. Church, Inc. v. Holmes, 60 App. D.C. 27, 46 F.(2d) 608 (1931); Holman v. Ryon, 61 App. D.C. 10, 56 F.(2d) 307 (1932).

Illinois: White v. Macqueen, 360 Ill. 236, 244, 195 N.E. 832, 98 A.L.R. 1115 (1935).

North Carolina: Hinton v. Pritchard, 120 N.C. 1, 26 S.E. 627, 58 Am. St. Rep. 768 (1897).

Wisconsin: Schroeder v. Arcade Theater Co., 175 Wis. 79, 106, 184 N.W. 542 (1921).

See Posner, Liability of the Trustee under the Corporate Indenture, 42 Harv. L. Rev. 198 (1928).

Where a lender pays money to a trust company to be paid to the borrower on the execution of a mortgage by him, the trust company, if it holds the money in trust, is trustee for both the lender and the borrower. See Civic Building & Loan Association's Appeal, 121 Pa. Super. 597, 184 Atl. 311 (1936).

[14]Hoffman, Burneston & Co. v. Mackall, 5 Ohio St. 124, 130-131 (1855).

See also Vance v. Lincoln, 38 Cal. 586 (1869); Neikirk v. Boulder Bank, 53 Colo. 350, 127 Pac. 137 (1912); McDonald v. Kellogg, 30 Kan. 170, 2 Pac. 507 (1883); Lance's Appeal, 112 Pa. 456, 4 Atl. 375 (1886); Catlett v. Starr, 70 Tex. 485, 7 S.W. 844 (1888).

APPENDIX 2.

The Appellee's Brief states:

"1. Section 70a of the Bankruptcy Act vests the trustee with title only to bankrupt's non-exempt property, and is not determinative of the time and manner of claiming such exemptions."

Section 70a of the Bankruptcy Act, which vests the trustee by operation of law with the title of the bankrupt as of the date of the filing of the petition, qualifies this vesting as follows: *"Except insofar as it is to property which is held to be exempt."*

The case of *White v. Stump,* 266 U.S. 310, 45 S.Ct. 103, is the controlling authority with respect to bankruptcy proceedings in the State of California. The decision involved a contended homestead exemption in the state of Idaho which has a similar law. In this Idaho case, no declaration was filed for record until after the filing of the bankruptcy. The district court, in the first instance, in reliance upon the case of *Brandt v. Mayhew,* 218 F.2d 422 (decided in 1914), held that the bankrupt was not precluded from claiming a homestead in California as exempt merely because, when the petition in bankruptcy was filed, he had not done all that is required by the state law to entitle him to the exemption, and further, that he may rightfully demand that the exemption be allowed where he has met the requirements of the state law within a reasonable time after the filing of the bankruptcy petition. The Circuit Court of Appeals for the 9th Circuit adhered to that decision and sustained the order of the district court. The Brandt case was of course relied heavily upon as the authority also for the same result in the state of Idaho with its similar exemption law.

However, the Supreme Court, in reversing the effect of the *Brandt v. Mayhew* case, said, in part, that the pertinent provisions of the bankruptcy law "show that the point of time which is to separate the old situation from the new in a bankrupt's affairs is the date when the petition is filed—Thus we have said that the law discloses a purpose 'intent' to fix the time of cleaveage, with special regard to the conditions existing when the petition is filed—It was not then exempt under the state law but was subject to levy and sale."

The appellee's brief makes the following comment on the *Brandt v. Mayhew* case (1914): "This is not the meaning of Section 70a. That section applies only to non-exempt property and does not deal with the time or manner of claiming exemption.

The *White v. Stump* case was further fortified by the United States Supreme Court in its case of *Myers v. Matley* decided in 1943. The exemption involved in this case was a selection of a homestead by a bankrupt in Nevada. The court had occasion to comment on the then new phraseology in the amendment of Section 70a (The Amendment changed the phrase "Insofar as it is not exempt" to "Except insofar as it is the property which is held to be exempt.") and states on page 625: "We conclude that the new phraseology in the amendment of Section 70a does not alter the principles applicable to the exemption of homestead property in bankruptcy."

In discussing the court's prior decision of *White v. Stump,* the court states, on page 625:

> "White v. Stump—involved the homestead exemption claimed pursuant to the law of Idaho under which the declaration of homestead was required

to be executed and acknowledged like a conveyance of real property and filed for record. The exemption arose when the declaration was filed and not before. Up to that time the land remained subject to execution and attachment like any other land; and where a levy was effected while the land was in that condition, the subsequent making and filing of a declaration neither avoided the levy nor prevented a sale under it."

(Note: An exception is noted here as between the Idaho and California law, in that in California an attachment does not bar the recording of a declaration of homestead.)

"This Court held that the Bankruptcy Act fixed the point of time which is to separate the old situation from the new in the bankrupt's affairs as the date when the petition is filed. *If the law of Nevada respecting homestead exemptions were like that of Idaho, or operated in the same way, White v. Stump would be in point.*"

Section 3315 of the Compiled Laws of Nevada define property which may be claimed as exempt as a homestead and permits selection by either the husband or the wife or both, by a declaration of intention in writing to claim the same.—"

"Section 8844 provides that the following property is exempt—etc."

Further from the opinion of Myers v. Matley, page 627:

"Historically, and under the theory of the present act, bankruptcy *has the force and effect of the levy of an execution* for the benefit of creditors to in-

> sure an equitable distribution among them of the bankrupt's assets. The trustee is vested not only with the title of the bankrupt but clothed with *the right of an execution creditor with a levy on the property which passes into the trustee's possession.*"

In this instance, the court was commenting upon Section 70c of the Bankruptcy Act which is the so-called strong arm provision of the Bankruptcy Act, which provides that "the trustee, as to all property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt could have obtained a lien by legal or equitable proceedings at the date of bankruptcy, shall deem vested as of such date with all the rights, remedies and powers of a creditor then holding a lien thereon by such proceedings, whether or not such a creditor actually exists."

This situation is, of course, hypothetical. The trustee can select a superior lien, in some instances an attachment lien, hypothetically selected, will suffice. In some, a recorded judgment lien will suffice and in an instance when a recorded judgment lien will not suffice, then, of course, an execution lien may be hypothetically selected. In fact, this is envisioned and expressly set forth in the *Myers v. Matley* case with the quotation above referred to: "The trustee is vested not only with the title of the bankrupt but clothed with the right of an execution creditor *with a levy on the property.*"

In California, an execution levied upon real property creates a lien thereon, cutting off all subsequent rights, claims, contentions, exemptions, etc. Civil Code Section 1241 states:

> "The homestead is subject to execution or forced sale in satisfaction of judgments obtained:

1) before the declaration of homestead was filed for record which constitute liens upon the premises."

Thus the trustee's lien by levy of the execution as referred to in the *Myers v. Matley* case would effectively block the declaration of homestead which was recorded subsequent to the date of bankruptcy at which time the trustee inherited the said rights to title and rights of lien.

In concluding the analysis of the Nevada law with respect to selection of homestead, the *Myers v. Matley* decision concludes, on page 627, that

"Examination of the Nevada cases relied on by the court below satisfied us that the settled law of the state entitles the debtor to his homestead exemption if the selection and recording occurs at any time before actual sale under execution.—In conformity with the principles announced in White v. Stump that the bankrupt's right to a homestead exemption becomes fixed at the date of the filing of the petition in bankruptcy and cannot thereafter be enlarged or altered by anything the bankrupt may do, it still remains true that, under the laws of Nevada, the right to make and record the necessary declaration of homestead existed in the bankrupt at the date of filing the petition as it would have existed in case a levy had been made upon the property. The assertion of that right before actual sale in accordance with state law did not change the relative status of the claimant and the trustee subsequent to the filing of the petition. The Federal Courts have generally so held and have distinguished White v Stump when the state law was

> similar in terms or in effect to that of Nevada." Citing Re *Rammmell,* 5 F.2d 326; *Clark v. Nirenbaum,* 8 F.2d 451; *McRae v. Felder,* 12 F.2d 554 and with a contra decision, *Georgouses v. Gillen,* 24 F.2d 292.

This latter case of the 9th Circuit determined that under Arizona law a homestead could not be selected after the filing of the bankruptcy proceedings. It cited as the authority therefor *White v. Stump,* 266 U.S. 310.

The second point set forth in the brief of the appellee is the following, to wit: IN ORDER TO ASCERTAIN WHETHER PROPERTY IS EXEMPT, ANALYSIS MUST BE MADE OF THE APPLICABLE STATE LAWS DEALING WITH EXEMPTIONS.

Under this point there is the appelle's comment on the case of *White v. Stump* with this observation:

> "Under the then existing law in Idaho, in the absence of bankruptcy, any creditor who had levied upon an attachment or execution would prevail over a subsequently filed homestead."

and dismissed the case entirely with the further statement:

> "Hence, in that case, since the bankrupt's creditors could have reached the land by levy and sale, the court held the property not to be exempt."

The bankrupt and his wife had title to the home and they caused the same to be placed in the name of the Title Insurance and Trust Company under a form of "trust" to secure money loaned by it to them, erroneously assumes that under Section 70c of the Bank-

ruptcy Act, sufficient and adequate liens by legal or equitable proceedings were not vested in the trustee which would reach his beneficial interest in the trust.

This error comes about through his point No. 3 which we will discuss hereinafter. The quotation from the *Myers v. Matley* case set forth on page 5 of Appellee's Brief adds considerably to the contention as asserted herein with the accentuation by the appellee of the following:

> "The trustee is vested not only with the title of the bankrupt, but clothed with right of an *execution creditor with a levy on the property which passes into the trustee's custody.*"

There is the further comment on page 5 under this same point of Appellee's Brief:

> "If that lien creditor has no rights under the state law, then neither does the trustee as to the property in question, and the property as exempt."

In the case of *Sampsell v. Straub*, 194 F. 2d 228, 9th Circuit, 1952 it is difficult for us to see how in any manner or by any means reference to the *Sampsell v. Straub* case can assist or fortify the contentions of the appellee. In supporting the contention that the rights of the trustee, the decision, on page 230, states:

> "On the other hand, the lien obtained by recording an abstract of judgment is described as a judgment lien. The California statute provides that a 'judgment or decree becomes a lien upon the filing of the abstract.' Code of Civil Procedure 674. And while recording is an independent step in the sense of being something voluntary beyond the entry of the judgment, it is incidental to the ju-

dicial process in the sense of a device to give a judgment particular effect. The judgment is the basic and fundamental source of right whether generally before recordation or by way of lien after recordation. —The context of Section 3, sub. a(3) and Section 67(a) rather clearly indicates that the California judgment lien should be regarded as a lien obtained by 'legal proceedings' within the meaning of these sections.

And the same includes 'a California judgment lien' among liens obtained by legal proceedings even though voluntary recordation is the essential final step in its creation—therefore, the assertion of this status of California judgment lienor by the trustee would be consistent with, though not essential, to the primary objection of Section 70(c). In brief, the policy of Section 70(c) permits the inclusive conception of liens by legal proceedings which the policy of Section 3a(3) and 67(a) require."

The final portion of the opinion on page 232 recites:

"That a California judgment lien though perfected only by voluntary recordation is a lien by legal or equitable proceedings within the meaning of Section 70(c).

Accordingly, we now vacate our order affirming the judgment of the district court and reverse the judgment."

Thus, the status of the trustee under Section 70(c) with the right of a recorded judgment lien was established. As we have noted hereinabove, the Supreme Court has gone one step further in the hypothetical legal proceedings and has equipped the trustee with an execution lien.

The third point as set forth in Appellee's Brief states: APPELLEE'S DECLARATION OF HOMESTEAD WHICH, IN THE ABSENCE OF BANKRUPTCY, WOULD HAVE PREVAILED IN CALIFORNIA AGAINST ANY LIEN CREDITOR AT THE TIME OF ITS FILING, WILL PREVAIL AGAINST THE TRUSTEE.

This statement is very seriously disputed. One would assume from this statement that in California it is impossible for creditors by legal proceedings to reach the beneficial interest of a trustee in real property and that is not the law. If we even assume that the conclusion is correct as to the particular feature of the California law (Code of Civil Procedure Section 674) with respect to the recording of an abstract of judgment where the judgment debtor has merely equitable title does not create a lien on the equitable interest by recordation of the abstract of judgment. The legal process, however, as against owners of beneficial interest in real property does not stop here. If so, this would create an absolute void.

The question is then, how in California does a creditor, by legal or equitable proceedings, with a recorded judgment against the defendant, reach the beneficial interest of the defendant in a real property trust.

The levy of an execution on real property creates a lien thereon and thus covers the beneficial interest of the defendant beneficiary. Thus it is not necessary to answer the various cases cited supporting the California law that the recording of an abstract of judgment does not create a lien upon real property held in trust for the defendant beneficiary, inasmuch as Code of Civil Procedure 674 does not specifically provide therefor.

We admit either the bankrupt or his wife could have filed a declaration of homestead on their home property which they were occupying, both before they transferred the same as well as after they transferred the same to the Title Insurance and Trust Company to hold in trust for them as a security for the loan which the Title Company made to the Chohons.

The case of *Poindexter v. Los Angeles Stone Co.,* 60 Cal. App. 686, holds that the recorded abstract of a judgment creates the lien only on legal interest in real property and does not create a lien created against the lien of a cestui que trust. This case however gives the answer to the query asserted by us hereinabove as to just how the interest can be reached and it states, on page 688 of the opinion:

> "It is true that execution may be levied against equitable as well as legal interest in real property—thus because the statute relating to execution expressly provides that a sale may be made of both real and personal property 'or any interest therein not exempt by law.' "

The case refers to a prior California case of *Belieu v. Power,* 54 Cal. App. 244 (1921) which determined that the judgment lien does not attach to the equitable interest of the defendant in real property. In commenting on Section 671 of the Code of Civil Procedure, page 246 states:

> "Property interests of every kind, whether real or personal, and every interest therein are subject to seizure under attachment or *levy on execution* unless exempt from execution (Section 542 and 688, Code of Civil Procedure). While many classes of property may be taken on execution, only two

> classes are subject to the lien of a judgment—real property owned by the debtor at the time of docketing and real property that he may afterwards acquire. While any interest in real property, legal or equitable, may be seized and sold under execution, only real property actually owned by the judgment debtor will support a judgment lien."

The trustee, by the provisions of Section 70(c) acquires the rights of an execution lien and thus the homestead declaration must be recorded *to be effective* before the advent of bankruptcy.

No. 18833

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

WILLIAM ROSS PHILLIPS,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLEE'S BRIEF.

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No. 18833

IN THE

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FOR THE NINTH CIRCUIT

WILLIAM ROSS PHILLIPS,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLEE'S BRIEF.

I.
JURISDICTION AND STATEMENT OF THE CASE.

The Federal Grand Jury for the Southern District of California returned Indictment No. 32056 on April 3, 1963, charging appellant in fifteen counts with causing the interstate transportation of counterfeit securities in violation of Title 18, United States Code, Section 2314. Appellant was tried by a jury and found guilty on all fifteen counts on April 22, 1963. On May 20, 1963, appellant was sentenced to ten years on each count to run concurrently, and on May 22, 1963, he gave notice of appeal.

The jurisdiction of the District Court was based upon Title 18, United States Code, Section 3231, and this Court has jurisdiction to entertain this appeal under the provisions of Title 28, United States Code, Sections 1291 and 1294.

II.
STATUTE INVOLVED.

Title 18, United States Code, Section 2314, provides in pertinent part:

> "Whoever, with unlawful or fraudulent intent, transports in interstate or foreign commerce any falsely made, forged, altered, or counterfeited securities, knowing the same to have been falsely made, forged, altered, or counterfeited;
>
> * * *
>
> "Shall be fined not more than $10,000 or imprisoned not more than ten years, or both."

III.
STATEMENT OF FACTS.

The testimony of Ruby Jean Shroyer, Gloria Lindauer, Julia Yenerich, Janette Wheeler, Everett Statford, Gay Bushee, and John Pepperling, employees of various banks in Arizona and California, established that the fictitious United California Bank personal money orders described in Counts One through Fifteen of the Indictment [Exs. 1-15] were cashed at various banks in the Phoenix, Arizona vicinity on about June 22, 1962, and were subsequently transmitted through normal banking channels to the United California Bank in Los Angeles, California. [R. T. 11-38.][1]

Mrs. Shroyer identified Robert Gene Roux, a subsequent Government witness, as the man who opened a savings account at the home office of the Valley National Bank in Phoenix on June 21, 1962, and obtained a savings passbook in the name of Walter G. Stewart.

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[1]R. T. refers to the Reporter's Transcript.

[R. T. 12-14.] This passbook was presented to Mrs. Lindauer as identification by a man who cashed a money order [Ex. 9] at her bank. [R. T. 17-18.]

Mrs. Yenetich identified George Edward Myers, another Government witness, as the man who cashed a money order [Ex. 2] at her bank, and at the same time presented as identification a driver's license [Ex. 19] in the name of Earl P. Lorcam. [R. T. 20-21.] Mrs. Wheeler also identified Myers as the man who attempted to cash a money order [Ex. 20] at her bank using the same driver's license [Ex. 19.] as identification, but who departed from the bank leaving the money order and driver's license behind. [R. T. 21-24.]

Roy Delgado Sanchez testified that appellant Phillips once asked him if he knew of, or could find, someone with a print shop in Tijuana, Mexico. Sanchez made inquiries and about a week later drove Phillips to Tijuana to meet a Bobby Gomez. Gomez introduced them to Horatio Sandoval, after which Phillips asked Sandoval if he could print checks and Sandoval replied that he could. Phillips asked Sandoval to print some checks for Desilu Productions. About a week later, Sanchez and Phillips returned to Tijuana where Phillips viewed the finished checks and said they were good. Phillips gave Sandoval some money and started back to Los Angeles in his own car. Sanchez saw the Border Patrol stop Phillips' car. Later, Phillips told Sanchez that the checks had been confiscated. [R. T. 40-46.]

Subsequently, Phillips and Sanchez visited Sandoval on several occasions concerning different kinds of checks that were being printed. Phillips talked with Sandoval about supplying certain printing equipment Sandoval didn't have, and later Phillips gave him the

equipment. [R. T. 46-48.] In about April, 1962, Phillips came to Sanchez' house with three different typewriters and a check writer. When Gomez brought a batch of checks there Phillips would fill in the faces of the checks using this equipment. [R. T. 48-49.]

Sometime in June, 1962, Gomez brought United California Bank personal money orders to Phillips at Sanchez' house. The amount was already printed on the face of these money orders. [R. T. 49-51.] Phillips mentioned that it would be difficult to pass the money orders without magnetic ink on the coded numbers at the bottom. He said he would give the money orders to his boys to pass out. [R. T. 76-77.]

Robert Gene Roux testified that he first met Phillips in about March, 1962, at a motel. On this occasion Phillips supplied Roux and a companion, Doyle Boss, with some checks and told them to cash them and make some money, which Roux did. [R. T. 79-82.] Afterward, Roux obtained some North America Aircraft checks from Phillips who said that he had obtained them in Tijuana. [R. T. 83.]

Once, in about May, 1962 Roux was with Phillips in the Covina, California area when Phillips entered a United California Bank and bought a money order. Phillips then returned to the car, opened a package and displayed a batch of money orders which he asked Roux to compare with the one just purchased. Roux noticed that they looked the same. He identified Exhibits 1 through 16 as being the type of money orders Phillips showed him in the car. Phillips told Roux that they would pass these money orders. [R. T. 83, 84.]

Subsequently, Phillips showed the money orders to George and Don Myers and plans were made for cashing them. The Myers brothers were to drive to Las Vegas, Nevada, and from there to Phoenix where Roux and Phillips would meet them. Phillips gave Don Myers some of the money orders. The next day Roux flew to Phoenix alone but failed to locate the Myers brothers so he returned to Los Angeles and contacted Phillips. Phillips and Roux then flew together to Phoenix and located George and Don Myers. [R. T. 90-91.]

In Phoenix, Roux opened a savings account at the Valley National Bank, and obtained an account book, as well as a map which showed the location of every branch of that bank in the city. George Myers rented a car which Don Myers and Phillips alternated in driving from one bank branch to another. George Myers and Roux were given a money order by Phillips, which they would cash. Upon returning the proceeds to Phillips he would give them each another money order to cash. While cashing the money orders, Roux used as identification, the savings account book, and a fictitious driver's license given him by Phillips. Once, in a gas station, Phillips stole a gasoline credit card bearing the name "John Swift" and said that it would make good identification. Phillips and Roux had arranged to split the money order proceeds 50-50. Roux got about $1400 from the Phoenix operation, and identified Exhibits 7, and 9 through 16, as money orders he endorsed and cashed there. [R. T. 92-95.]

Roux later traveled to other cities, such as St. Louis, Missouri, Kansas City, Missouri, Kansas City, Kansas, Oklahoma City, Oklahoma, and Reno, Nevada, to cash

money orders which Phillips had given him. In a hotel in St. Louis, Roux saw Phillips in possession of some of the money orders. Roux gave most of the money from those he cashed to Phillips. [R. T. 96-98.]

George Edward Myers testified that in about June, 1962, his brother Donald introduced him to Phillips in a Hollywood, California apartment. On this occasion, Phillips was seated by a coffee table and was punching out IBM holes in United California Bank personal money orders similar to Exhibits 1 through 16. George Myers was told that he would cash these money orders. [R. T. 132-133, 148.]

A day or two later George Myers and his brother went around cashing money orders. At one bank, an employee's suspicion caused George to walk out and leave a money order and a fictitious driver's license behind. George went to a motel to wait for his brother, but was joined there by Phillips who asked him if there was anything about the money order that made the bank employee suspicious of it. At this time, George gave Phillips a savings account book that he had been using as identification. [R. T. 134-136.]

A short time later, in West Covina, George and his brother Donald met Phillips and Robert Roux. They discussed an out-of-town trip to cash checks and planned to meet later in Phoenix. George and Donald Myers drove to Las Vegas and from there went to Phoenix where they met Roux and Phillips. George rented an automobile and the four men drove about the city from bank to bank—most of which were branches of the Valley National Bank. Phillips and Donald took turns driving; George and Roux were in the back seat. George

was given a money order to cash, and when he gave the proceeds to Donald, the latter would give him another money order. George was given about 25% of the money he took in. For identification, he used a fictitious driver's license given him by Donald. George Myers identified Exhibit 19 as the license, and Exhibits 1 through 6, and 8, as money orders he endorsed and cashed in Phoenix. [R. T. 136-144.]

George Myers traveled to other cities, such as Reno, Philadelphia, and St. Louis to cash money orders. Phillips was with him in St. Louis and Reno. [R. T. 145-146.]

Mrs. Jo Ann Roux, wife of Robert Roux, testified that she first met Phillips in West Covina shortly after her husband was arrested in a motel, and she was detained for questioning. Phillips picked her up in his car a short distance from the police station and asked why Gene Roux and Fred Holzer had been arrested. That evening, Phillips drove Mrs. Roux to Los Angeles and on the way he explained his check passing activity by stating that he had fictitious checks printed in Tijuana, and that he also had phony I-D cards and driver's licenses. Phillips named several people who were passing checks for him, including Fred Holzer and Charles Abshire. [R. T. 153-158.]

At a later time, when her husband was in jail, Mrs. Roux went to live at Phillips' house for a little over a month. During that time she overheard conversations about a man named Craig in New York, and that when Phillips went to New York he would take some checks with him. Phillips, and later Mrs. Phillips did leave for New York. On his return Phillips was very disgusted and said that everything was a failure because Craig

had taken off with some money, and that Craig had been arrested. [R. T. 159-161.]

Mrs. Roux heard Phillips explain various aspects of his check-passing scheme to Donald Myers on at least two occasions. [R. T. 161-162.] While at Phillips' home, Mrs. Roux received calls from a deep voiced male who Mrs. Phillips identified as a detective that worked for Phillips. [R. T. 162-163.] Mrs. Roux once accompanied her husband to St. Louis, and saw Phillips in a hotel room there when he had a briefcase containing blue checks like Exhibits 1 through 16. [R. T. 163-164.] Once when Mrs. Roux was arguing with her husband about his involvement in the check ring, Phillips told her she couldn't scare him and that he could have her taken care of. [R. T. 166.]

Mr. A. M. Barr, a Los Angeles Police Officer assigned to forgery investigation testified that on October 18, 1962, in Monterey, California, he had a conversation with Phillips, during which Phillips admitted that the United California Bank personal money orders were printed for him in Tijuana and were passed in Phoenix by Roux and Don Myers. Later, Phillips said it was not Don but George Myers. [R. T. 196.] Phillips admitted that he had received part of the proceeds from the money orders that were cashed there and that the same operation had been conducted in St. Louis and New York. Phillips also said that Officer Irwin had been hounding him for money, and that Irwin would have to share the blame. [R. T. 188-192.]

Phillips also told Barr that he didn't make much money from the check operation because he had to pay bondsmen and attorney fees, and that he also paid Irwin for police protection. In particular, Phillips said he paid Irwin $5,000 to get himself released from custody in San Diego. [R. T. 192-194.] Phillips said that Irwin told him where fictitious checks could safely be passed. [R. T. 195.] Phillips never mentioned that Irwin had threatened to return him to prison as a parole violator if he didn't cooperate with Irwin. [R. T. 200.]

John A. Kelleher, special agent of the F.B.I., testified that he interviewed Phillips on October 18, 1962, in Monterey, California, at which time Phillips signed a document [Ex. 25] confessing that he obtained about $270,000 in fictitious United California Bank personal money orders from a printer in Mexico, and that he went to Phoenix with George Myers and Roux where they were cashed. He also admitted that he received part of the proceeds. [R. T. 209-211.]

Appellant Phillips testified in substance that he was forced into managing the fictitious check operation against his will by the threats of Police Officer Irwin of West Covina to return Phillips to prison as a parole violator if Phillips did not comply with Irwin's wishes. [R. T. 218-244.] He admitted having the checks printed in Mexico, and distributed in various cities around the country; he also acknowledged that he received money from this activity. Phillips named at least six dif-

ferent kinds of checks that were used by the check ring. He acknowledged that he supplied fictitious identification for his check passers, and that he knew that the cashing in other states of checks drawn on California banks would result in the interstate transportation of such checks. [R. T. 244-256.] Phillips admitted he never told his parole officer, the F.B.I. or any other federal officer that Irwin had threatened him. [R. T. 260, 264.] He named about a dozen persons as being members of his check ring. [R. T. 290-291.] Phillips acknowledged having been convicted of five prior felonies. [R. T. 293-299.] Mrs. Janet Phillips, wife of appellant, testified in substance that Officer Irwin was the one behind the check ring. [R. T. 301-317.]

It was stipulated that Officer Hart of the Baldwin Park, California, Police Department would testify that in the Spring of 1962 he and other officers arrested Phillips and his wife on check charges, but released them when Irwin came to their house and said that Phillips was working undercover for him. [R. T. 317-318.]

Joseph Cantrelle testified that Phillips asked him to listen to a telephone conversation with Officer Irwin. Thereafter Phillips dialed the West Covina Police Department and told Irwin he didn't want to go to Arizona to pass checks because it would be a federal violation. Irwin told Phillips he had better go if he valued his life and his freedom. [R. T. 324-327.]

In rebuttal, Robert Roux testified that he had never heard Phillips mention that Irwin was forcing him to engage in check passing activity, but that Phillips had

told him that he was paying Irwin for information. [R. T. 333.]

Argument in the case concluded on Thursday afternoon, April 18, 1963. On Friday morning, April 19, 1963, appellant did not appear in Court. Mrs. Phillips was called as a witness by the Court in the jury's absence, and testified that Phillips had accompanied her to the courthouse and told her to go on in and he would be right there. [R. T. 379-381.] The Court continued the case until Monday morning, April 22, 1963, because of the possibility that appellant had been unavoidably absent. [R. T. 382.] On Monday, April 22, 1963, appellant was again absent when Court convened. Appellant's bail bondsman, through appellant's attorney, advised the Court that he had heard from Phillips over the week-end, and that Phillips had said he would be present in Court on Monday morning, April 22, 1963. [R. T. 389.] The Court thereafter found that appellant voluntarily absented himself from the trial. [R. T. 413.]

IV.

SUMMARY OF ARGUMENT.

A. The Jury was Correctly Instructed on the Defense of Coercion.

B. The Court Properly Permitted the Trial to Proceed in Appellant's Absence.

C. The Argument of Government Counsel was Unobjectionable.

D. Evidence Bearing Upon Appellant's Offenses or His Motive, Intention, Knowledge, Plan and Design, or Showing the Absence of Coercion, Was Properly Received.

V.

ARGUMENT.

A. The Jury Was Correctly Instructed on the Defense of Coercion.

Since Appellant's Brief fails to comply with this Court's Rule 18(2)(d) pertaining to specification of error relating to instructions, the following facts are here set forth: When the Government's proposed instruction on the defense of coercion was first submitted to the Court, the following conversation took place:

> "Mr. Parsons: I think we would have to object to No. 12, the instruction under duress.
>
> The Court: Why?
>
> Mr. Parsons: I think there is some confusion in the law with reference to whether or not a threat of prosecution of imprisonment is not sufficient coercion. I think that is such a limitation on it—from the circumstances in this case I think the jury might well infer that most anything could have happened to this man, from the testimony that he has given, and I must therefore respectfully object to the giving of instruction 12." [R. T. 270-271.]

Defense counsel offered no alternative instruction on the defense of coercion and the Court gave the following instruction to the jury:

> "Duress or coercion does not excuse the commission of a crime, unless the compulsion is immediate, cannot be reasonably escaped, and is of such a nature as to induce a well grounded apprehension of death or serious bodily injury if the crime is not committed. A threat of prosecution or imprisonment is not sufficient coercion to excuse the commission of a crime." [R. T. 406.]

Before the jury retired the following inquiry was made and answer given:

> "The Court: Has the defendant any objection to the giving of any instruction or the omission of any instruction?
>
> Mr. Parsons: None." [R. T. 407.]

Rule 30, Federal Rules of Criminal Procedure, states that: "[n]o party may assign as error any portion of the charge . . . unless he objects thereto before the jury retires to consider its verdict, stating distinctly the matter to which he objects and the grounds of his objection." Painstaking compliance with this rule is required.

Lyons v. United States, 325 F. 2d 370 (9th Cir. 1963);

Brown v. United States, 222 F. 2d 293 (9th Cir. 1955);

Enriquez v. United States, 188 F. 2d 313 (9th Cir. 1951).

Therefore, the allegation of error as to the instruction in question should not be considered on appeal.

However, even if the matter is deemed to be subject to appellate review, it is obvious that the instruction given was a correct statement of the law. In *Iva Ikuko Toguir D'Aquino v. United States,* 192 F. 2d 338 (9th Cir. 1952); *cert. denied,* 343 U. S. 935 (1952), the Court of Appeals considered appellant's claim that the following instructions given upon the subject of coercion were erroneous:

> "In other words, ladies and gentlemen of the jury, this coercion or compulsion that will excuse a criminal act must be present, immediate and [im]pend-

> ing, and of such a nature as to induce a well grounded apprehension of death or serious bodily injury if the act is not done.
>
> * * * * *
>
> . . . [I]t is not sufficient that the defendant thought that she might be sent to a concentration or internment camp. . . ." (Note 11, p. 358.)

The Court noted that the instruction in question was almost identical to that approved in *Gillars v. United States,* 182 F. 2d 962 at 976, note 14 (D.C. Cir. 1950), and said:

> "The charge was a correct statement of the law upon this subject. *United States v. Vigol,* 2 Dall 346, 2 U.S. 346, 1 L.Ed. 409; *Respublica v. McCarty,* 2 Dall 86, 2 U.S. 86, 1 L.Ed. 300; *Shannon v. United States,* 10 Cir., 76 F.2d 490; *R.I. Recreation Center v. Aetna Casualty & Surety Co.,* 1 Cir., 177 F.2d 603, 12 A.L.R. 2d 230." (192 F. 2d at 358) [Italics added]

Counsel for appellant cites no cases which support his contention that a threat of any kind may be sufficient to establish a defense of duress. His argument, that the law respecting a defense of duress in civil contract cases should also be applied to such a defense in criminal cases, is not even supported by the half dozen law review notes and articles cited, and completely overlooks the policy considerations which require that persons resist coercion to commit crime to a greater degree than coercion to contract, before they are excused from responsibility.

Appellant's brief (p. 18) states that Phillip's testimony was credible, and indicates that the Court's in-

struction on duress precluded the jury from considering it. Both propositions are incorrect. The jury *was* permitted to consider appellant's story in the light of the instruction given. Further, on appeal, the evidence does *not* consist of that to which appellant and his witnesses testified, but of the evidence at trial taken in the light most favorable to the Government, together with all reasonable inferences which may be drawn therefrom. *Glasser v. United States,* 315 U. S. 60 (1942); *Bolen v. United States,* 303 F. 2d 870 (9th Cir. 1962); *Young v. United States,* 298 F. 2d 108 (9th Cir. 1962); *cert. denied* 370 U. S. 953 (1962); *Benchwick v. United States,* 197 F. 2d 330 (9th Cir. 1961; *Teasley v. United States,* 292 F. 2d 460 (9th Cir. 1961); *Sandez v. United States,* 239 F. 2d 239 (9th Cir. 1956).

B. The Court Properly Permitted the Trial to Proceed in Appellant's Absence.

Rule 43 of the Federal Rules of Criminal procedure provides in part that "[i]n prosecutions for offenses not punishable by death, the defendant's voluntary absence after the trial has been commenced in his presence shall not prevent continuing the trial to and including the return of the verdict."

In *Cross v. United States,* 325 F. 2d 629, 631 (D.C. Cir. 1963), it was said that the purpose of this provision "is to prevent frustration of a trial in progress by the escape or absconding of the defendant."

Appellant's brief (p. 20) mistakenly states that neither the Government nor the Court made any effort to determine why Phillips was absent from the trial, and that the Court's finding that appellant's absence was voluntary was not supported by any fact.

Actually, when appellant failed to appear at 9:45 a.m. on Friday, April 19, 1963, as instructed at the conclusion of court the day before, the convening of court was delayed for an hour. [R. T. 375, 379.] Thereafter, the Court convened and held a hearing to determine why appellant was absent, during which Mrs. Phillips testified under oath that Phillips had accompanied her to the courthouse that morning and had said he would be inside shortly. [R. T. 381.] Because of the possibility that appellant might have been unavoidably absent, the Court then continued the case for three days to Monday, April 22, 1963. [R. T. 381, 382.] At the request of appellant's attorney and bondsman, the Court forfeited appellant's bond and issued a bench warrant for his arrest on April 19, 1963. [R. T. 382, 383.] Defense counsel advised the Court that the bondsman would make every effort to locate Phillips [R.T. 382], and the Court asked that information as to his whereabouts be relayed to the F.B.I. [R. T. 410], who had an all points bulletin out for him [R. T. 413]; but no one was able to locate appellant.

On Monday, April 22, defense counsel advised the Court that appellant had contacted his bondsman over the week-end, and told him that appellant would be present in court at that time; however, appellant did not appear. Defense counsel also informed the Court that appellant had failed to make a required appearance in a State court that same morning. [R. T. 389, 409.]

Under these circumstances, and since appellant never communicated with his counsel, the Court, or the Government as to his absence from the trial, the Court found that the absence was voluntary. [R. T. 412-413.]

It should be pointed out that when a defendant is in custody during trial, the Government has a duty to see that he is brought into court so that he may be present during the trial. *Cross v. United States,* 325 F. 2d 629 (D.C. Cir. 1963); *Evans v. United States,* 284 F. 2d 393 (6th Cir. 1960). However, when a defendant is on bond during a trial, it would seem that he has some obligation to appear at the times appointed by the Court, or if he is unable to do so, to communicate with the Court or counsel concerning his absence if at all possible. This, appellant never did.

Under the circumstances, the Court did all that it could to determine why Phillips was absent. Until Phillips was located and questioned, there was no further way to determine whether his absence was voluntary or not. To require the Court to await apprehension of an apparent fugitive before finding that his absence was voluntary and proceeding with the trial would permit the frustration of a trial in progress by the escape or abscondance of the defendant contrary to the purpose of Rule 43.

Since the Appellant's Brief (p. 20) goes outside the record in stating that appellant was absent from trial because he was kidnapped, the Government wishes to point out that the Probation Officer's pre-sentence report on appellant indicates that Phillips was apprehended by police, several days after his disappearance, in a Hollywood motel room that was being used as a base for check passing activity, and at that time, Phillips had fictitious checks and identification in his possession.

C. The Argument of Goverment Counsel Was Unobjectionable.

Only in cases of clear abuse by a district attorney should a conviction be set aside because of improper argument. *United States v. Redfield,* 197 F. Supp. 559 (D. Nev. 1961), *aff'd* 295 F. 2d 249 (9th Cir. 1961), *cert. denied* 369 U. S. 803 (1962); *Brennan v. United States,* 240 F. 2d 253 (8th Cir. 1957), *cert. denied* 353 U. S. 931 (1957); *Weiss v. United States,* 122 F. 2d 675 (5th Cir. 1941), *cert. den.* 314 U. S. 687 (1942). For example, in *Iva Ikuko Toguri D'Aguino v. United States,* 192 F. 2d 338 (9th Cir. 1952); *cert. denied* 343 U. S. 935 (1952), it was held that the Government's argument that the prosecution should serve as a warning to others that they cannot desert their country and adhere to the enemy with impunity did not constitute such misconduct as to require a new trial.

Appellant's brief (p. 8) states that "prosecution counsel argued to the jury that since appellant's accomplices had been convicted, appellant also ought to be punished," and cites in support of this contention two short quotations from the Government's argument which are taken out of context, and one of which has been carefully edited. (Appellant's Br. p. 21.) Nothing could be further from the truth.

The first quotation was taken from among the Government's comments on the credibility of Phillips' story that he had engaged in his check activity only because Officer Irwin had threatened to return him to prison as a parole violator, during the course of which the prosecutor stated:

> "The defendant has served three years eight months of a five year sentence. All he has left is

a year and four months. But he is risking all this nation-wide check activity to stay out of jail a year and four months. Do you believe that?

"Also, you heard the list of names I read off this morning, and he said 'yes,' 'yes,' 'yes,' 'he worked for me,' and so forth.

"Maybe you didn't count them. Mr. Phillips said there were eleven, he admitted to eleven, and the twelfth man, Mr. Boss, or White, I forget his last name, was denied by Mr. Phillips. But Mr. Roux says to the contrary. Anyway, the vast portion of those I think Mr. Phillips stated were in jail. So here Mr. Phillips, he is going to keep out of jail by passing checks all over the country, but he gets the whole ring in jail *and himself in trouble as well.*[2] Mr. Phillips, of course, has told different stories before." [R. T. 367-368.]

The second quotation is carefully lifted from the Government's comments about whether the whole nature of the fictitious check operation shed any light on whether it was set up by an unwilling victim of Officer Irwin's threats, or was the creation of a man eager to make some easy money. In the course of these remarks, the prosecutor said:

"I think the clincher on all that is just look at the operation and ask yourself one question: Is this the setup of a man who doesn't have his heart in his work? And look at it. The work of an unwilling, reluctant man who is dragging his feet every step of the way?" [R. T. 369.]

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[2]The italicized portion of this sentence was conveniently omitted from appellant's quotation.

Thereafter, the prosecutor recounted the various facets of the check operation including the printing operation that Phillips had set up in Mexico, the couriers who delivered the checks, the numerous types and amounts of checks printed, the dozen or more persons recruited to pass the checks, the fictitious identification supplied by Phillips, the nationwide scope of the passing operation, the fact that Phillips usually got at least 50% of the proceeds, Phillips' role in the operation, and the police protection, attorneys, and bail bondsmen who were said to be available to the ring. [R. T. 369-372.] The prosecutor concluded that "[i]t is not a fly-by-night scheme that Mr. Irwin kicked Mr. Phillips into. A well thought out master plan by the master planner, namely William Ross Phillips." [R. T. 372.]

The immediate context from which the remarks objected to were taken is as follows:

> "What was Phillips' role in this operation? Well he took care of the printing, he took basic care of the idea. He took care of the cashing, in the sense that he furnished them one check at a time and got the money back. I suppose—remember Craig in New York ran off with the proceeds. Maybe it is not good to hand out 20, you have got to give them one at a time. Phillips was cautious. He handed out one at a time and took the proceeds and gave another one. He never signed any of them. He never passed any of them. He did some typewriting that is hard to identify, but he never signed or cashed any of them. *Phillips is in the background. He is protecting himself.*

Let these other twelve guys get in jail, like they are, but Phillips, no[3] Remember, too, the interesting comments you heard about attorneys and bail bondsman for the people who are arrested." [R. T. 371-372.]

The above quotation consists of argument to establish that the check activity was conducted willingly by Phillips with the care and planning of a business operation, and that it was not the reluctant result of threats by Officer Irwin. Defense counsel made no objection to any remarks of the Government, and therefore an allegation of error should not be considered on appeal. *Kreinbring v. United States,* 216 F. 2d 671 (8th Cir. 1954). At no time did the Government argue that because his accomplices were in jail, Phillips should also be punished.

It is to be noted that although the prosecution never made the argument that appellant alleges, the defense did argue, in effect, that since Irwin was not prosecuted, Phillips should not have been prosecuted either. [R. T. 351-352.]

D. Evidence Bearing Upon Appellant's Offenses, or His Motive, Intention, Knowledge, Plan and Design, or Showing the Absence of Coercion, Was Properly Received.

Rule 18(2) of the Rules of the United States Court of Appeals for the Ninth Circuit provides in pertinent part that:

"This [appellant's] brief shall contain in order here stated—

* * * * *

[3]Only the italicized portion is quoted by appellant.

"(d) In all cases a specification of errors relied upon which shall be numbered and shall set out separately and particularly each error intended to be urged. When the error alleged is to the admission or rejection of evidence the specification shall quote the grounds urged at the trial for the objection and the full substance of the evidence admitted or rejected, and refer to the page number in the printed or typewritten transcript where the same may be found."

Inasmuch as appellant's brief does not comply with the requirements of Rule 18(2)(d), the Government sets forth the following:

After Roy Sanchez testified without objection that he had seen Phillips stopped by the Border Patrol and had notified Mrs. Phillips about it [R. T. 44-45] the following occurred:

"Q. What did you tell her and what did she tell you? We offer this as the statements of a partner to the common scheme and plan, which we will establish.

"Mr. Parsons: We object on the ground it is hearsay, and at this time I move to strike the testimony so far as irrelevant, incompetent and immaterial to any issue set forth in this case. It is not material. I have not heretofore objected, because I had to, of necessity, hear it. It is immaterial to any issue here.

"The Court: The motion is denied. The objection is sustained.

"Mr. Nissen: As to what, sir?

"The Court: The objection to this conversation with his wife." [R. T. 45.]

After Robert Roux had testified without objection that he had traveled to cities other than Phoenix to cash money orders furnished by Phillips [R. T. 96] the following occurred:

"Q. Let's take them one at a time. Did you ever see Mr. Phillips in St. Louis while you were there?

Mr. Parsons: To which we object as immaterial, irrelevant, to anything charged in this case.

Mr. Nissen: We offer it as scheme and plan. Since our indictment charges the causing. We are trying to show the relationship between Mr. Phillips and this witness who admits his participation.

The Court: The objection is overruled.

* * * * *

A. Yes sir. We flew to St. Louis, George Myers and I and our wives, flew on a Saturday night. Mr. Phillips was supposed to come to St. Louis and meet us Sunday, but something went wrong where he didn't get there, I believe it was, until Tuesday morning. And we all met at the Lennox Hotel in St. Louis. And we tried to cash some checks in St. Louis, Mr. Phillips and I, and George Myers and his brother Don Myers, but we didn't cash any in St. Louis.

Q. What kind of checks were those.

A. United California money orders. I cashed one check at the Lennox Hotel." [R. T. 96-97.]

The two objections quoted above are the only ones mentioned in appellant's specification of error number 5. (Appellant's Br. p. 11, lines 10-12.) The first objection was sustained, although defense counsel's mo-

tion to strike testimony previously received without objection was denied. This motion was properly denied inasmuch as the prior testimony concerned Phillips' establishment of the printing operation in Mexico which later produced the United California Bank money orders that were cashed in Phoenix by Roux and George Myers; and this testimony was clearly material.

The second objection pertained only to whether Roux had seen Phillips in St. Louis. Substantially the same evidence was elicited from George Myers without objection. [R. T. 145-146.] In fact both Roux and Myers testified without objection to traveling to various cities in order to cash money orders [R. T. 96-97, 145-146] and defense counsel questioned them as to various aspects of these trips not gone into on direct examination. [R. T. 105, 117, 120, 149-150.] In view of this, appellant should not be able to attack the admission of this evidence on appeal. *Gilbert v. United States,* 307 F. 2d 322 (9th Cir. 1962); *Ramirez v. United States,* 294 F. 2d 277 (9th Cir. 1961).

Furthermore, the testimony appellant complains of (Appellant's Br. p. 10, line 15, through p. 11, line 6) would have been admissible even over a defense objection. Sanchez' testimony about Phillips' arranging the Mexican printing operation was admissible as a necessary aspect of establishing that the United California Bank money orders referred to in the indictment were counterfeited and were traceable to Phillips. *Kobey v. United States,* 208 F. 2d 583 (9th Cir. 1954); *Schwartz v. United States,* 160 F. 2d 718 (9th Cir. 1947).

Testimony as to Phillips' check ring activities in other cities, similar to and at about the same time as his operation in Phoenix, were admissible to show

motive, intention, knowledge, plan and design, and to negative a defense of coercion. *Carr v. United States,* 317 F. 2d 409 (9th Cir. 1963); *Carbo v. United States,* 314 F. 2d 718 (9th Cir. 1963); *Enriquez v. United States,* 314 F. 2d 703 (9th Cir. 1963); *Bible v. United States,* 314 F. 2d 106 (9th cir. 1963); *Stewart v. United States,* 311 F. 2d 109 (9th Cir. 1962); *Corey v. United States,* 305 F. 2d 232 (9th Cir. 1962), *cert. denied* 371 U. S. 956 (1962); *Benchwick v. United States,* 297 F. 2d 330 (9th Cir. 1961); *Medrano v. United States,* 285 F. 2d 23 (9th Cir. 1960), *cert. denied* 366 U. S. 968 (1961); *Sachs v. United States,* 281 F. 2d 189 (9th Cir. 1960), *cert. denied,* 364 U. S. 909 (1960).

Mrs. Roux's testimony that Phillips threatened her when she was arguing with her husband over Roux's involvement in the check ring was relevant to show his motive and intention, and whether he was acting under duress. *Stewart v. United States,* 311 F. 2d 109 (9th Cir. 1962), and cases cited in paragraph above. The jury was informed that this was the manner in which Mrs. Roux's testimony was relevant, when the Government said in final argument: "And is a person who is in business against his will going to go around threatening people? Or would he say, 'I am sorry, I don't want to be in this any more than you do, but I have got to save my neck.' "

VI.
CONCLUSION.

For the reasons stated above, the judgment of conviction should be affirmed.

Respectfully submitted,

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Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

David R. Nissen

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

No. 18,834

JESS GREEN, and THE NEZ PERCE INDIAN ASSOCIATION,
Plaintiff-Appellants

v.

ANGUS A. WILSON, ALBERT EZEKIEL, MOSES THOMAS, PHIL TYPES, ALLEN SLICKPOO, EARL M. GOULD, FRANK PENNEY, RICHARD HALFMOON and HARRISON LOTT,
Defendant-Appellees

On Appeal From An Order of The United States District Court For The District of Idaho, Central Division

BRIEF FOR DEFENDANT-APPELLEES

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BRIEF FOR DEFENDANT-APPELLEES

JURISDICTIONAL STATEMENT

The case was decided by the Court below by granting the motion of defendants-appellees to dismiss the complaint on the grounds, *inter alia,* that the court lacked jurisdiction over the subject matter and over two indispensable parties. Appellees' contentions that the District Court lacked jurisdiction are set forth in detail in the body of this Brief.

This Court has jurisdiction to review the judgment of the court below under 28 U.S.C. § 1291.

SUMMARY OF ARGUMENT

In this action appellants seek judicial intervention to upset the institutions of self-government established by the members of the Nez Perce Tribe of Idaho and recognized and approved by the Legislative and Executive Branches.

The principal allegations of the complaint are (1) that the Revised Constitution and By-Laws, under which the Tribal government is constituted, are illegal and unconstitutional, and (2) that the elected officers of the Tribe are misusing tribal funds by expending them upon such economic and social development projects as sewers and sanitary water facilities, community buildings for youth recreation and adult education, and the possible development of tourist facilities. The complaint seeks to compel appellees to restore these funds to the Tribal treasury so that they may be distributed per capita to appellants and other members of the Tribe.

The appellees moved the District Court to dismiss the complaint on four separate grounds, each of which was adequate to support the motion. The District Court granted the motion to dismiss. In this Brief appellees have presented each of the four grounds argued in the court below.

1. The Complaint Fails to State a Claim Upon Which Relief Can Be Granted

Those portions of the complaint which challenge the Revised Constitution and By-Laws fail to state a cause of action.

The forms and procedures of Indian tribal self-government are not subject to scrutiny in the courts. The rule uniformly adhered to is that the judiciary accepts the decisions of Congress or the Executive with respect to recognition of Indian tribal governments and their internal rules of administration. The Revised Nez Perce Constitution was approved by the Department of the Interior and the

appellees, as the duly elected governing body thereunder, are recognized by that Department.

Those portions of the complaint which allege that the Tribal officials abused their discretion by expending Tribal funds for community development projects also fail to state a claim upon which relief can be granted. The Revised Constitution clearly grants to the elected Tribal officials authority to expend Tribal funds for any purpose which will "promote and protect the health, education and general welfare of members of the Tribe." There is no precedent for a court substituting its judgment for that of tribal officials, acting with the approval of the Secretary of the Interior, as to the wisdom of specific expenditures of tribal funds.

2. The Court Below Lacked Jurisdiction Over the Subject Matter

The only possible ground of jurisdiction in the Court below is the existence of a question "arising under the Constitution, laws or treaties of the United States." An examination of the complaint demonstrates that no rights arising under the Constitution, laws or treaties of the United States are asserted.

Many previous cases involving suits by individual Indians against their tribes have been dismissed for lack of a Federal question. The courts have repeatedly held that disputes involving the use and distribution of tribal property must be resolved by internal tribal law and not in Federal courts.

3. The Complaint Failed to Join an Indispensable Party—the Nez Perce Tribe

This suit is in law and in fact an action against the Nez Perce Tribe. The named defendants were the nine elected officials of the Tribe. The complaint prays that the tribal Constitution be declared illegal and that all further expenditures of tribal funds be halted.

In similar cases where members of an Indian tribe have sought to sue a tribal officer in his official capacity, the courts have held the tribe to be an indispensable party. Since the Nez Perce Tribe is immune from suit, and cannot be joined, the complaint had to be dismissed.

4. The Complaint Failed to Join an Indispensable Party—the United States

Both major allegations of the complaint so affect the vital interests of the United States that it must be joined as a party. The Revised Constitution and By-Laws were approved by the Secretary of the Interior and constitute the working agreement between the United States and the Nez Perce Tribe concerning the manner in which the affairs of the Tribe shall be conducted. Any action to set that agreement aside should not proceed without the United States as a party.

The allegations of misuse of tribal funds also affect the vital interests of the United States. The expenditures specified in the complaint were made with the approval of the Secretary of the Interior, acting in accordance with Congressionally established procedures. The Secretary has encouraged the Tribe to expend its judgment funds for useful, community development projects of the type of which appellants complain.

To halt the expenditure of Tribal trust funds, and to declare illegal the expenditures already made with the approval of the Secretary, is clearly to frustrate the program of the United States for the development of the Nez Perce Tribe and so affect its vital interests that the United States is an indispensable party.

For all of the foregoing reasons, any one of which is sufficient, the District Court was clearly correct in dismissing the complaint.

ARGUMENT

I. THE FACTUAL BACKGROUND

This suit was commenced by an individual member of the Nez Perce Tribe and an association which is said to consist of "enrolled, unemancipated members of the Nez Perce Indian Tribe." R. 4. The suit seeks to enjoin the members of the elected governing body of the Tribe, the Nez Perce Tribal Executive Committee, from carrying out community development projects engaged in by the Nez Perce Tribe in conjunction with a number of Federal agencies, and further seeks to require these Tribal officials to distribute all Tribal funds among the members per capita.

The Nez Perce Tribal Executive Committee was first constituted under a Constitution and By-Laws, approved by the Bureau of Indian Affairs on April 2, 1948, and ratified by the Tribe on April 30, 1948. The 1948 Constitution and By-Laws are set forth in Appendix A to this Brief. Article IX of this Constitution permitted amendments by majority vote of the qualified voters of the Tribe or majority vote of the General Council. *Id.* at p. 4a. Article II, Section 6 of the By-Laws fixed the quorum requirement of the General Council at fifty members. *Id.* at p. 6a.

After more than a decade of operation under the 1948 Constitution, members of the Tribe took steps to overhaul that document. In 1959 a special Amendments Committee was established, which frequently conferred with officials of the Bureau of Indian Affairs on proposed revisions of the Tribe's organic document. R. 21. After two years of discussion and advance clearance by the Bureau of Indian Affairs, the comprehensive Revised Constitution and By-Laws were submitted to and were approved by the Tribal General Council on May 6, 1961. R. 21. At that meeting 132 members were present and voting. R. 20. The new Constitution was approved by the Commissioner of In-

dian Affairs on June 27, 1961. R. 22. As the Nez Perce Tribe had not adopted the Indian Reorganization Act, sometimes called the "Wheeler-Howard Act" (Act of June 18, 1934, 48 Stat. 984), the Commissioner approved the document under the powers vested in him by the provisions of 25 U.S.C. § 2. R. 23.

The root cause of this suit is the money made available to the Nez Perce Tribe and to Nez Perce Indians on the Colville Reservation in the State of Washington under judgments entered by the Indian Claims Commission. These judgments, entered in 1959 and 1960, totaled $7,157,605. R. 4. By appropriate legislation, Congress authorized the division of the funds between the two groups in stated proportions and provided that the money may be "advanced or expended for any purpose which is authorized by the respective tribal governing bodies *and approved by the Secretary of the Interior.*" Act of April 24, 1961, 75 Stat. 45, herein referred to as Public Law 87-24 (emphasis supplied).

Following the enactment of Public Law 87-24, the Nez Perce Tribal Executive Committee entered into discussions with the Secretary of the Interior concerning an acceptable plan for utilization of its share of the judgment funds. In accordance with a resolution of the Tribal General Council, the Tribal officials proposed the per capita distribution of most of the judgment funds to the members of the Tribe. The Department of the Interior, on the other hand, took the position that the bulk of the funds should be used to develop economic opportunities on the Nez Perce Reservation.

The Department's position on per capita payments was defined by the Task Force on Indian Affairs, appointed by Secretary of the Interior Stewart L. Udall in 1961:

> Another potential source of capital for resource development is the judgment money from cases now pending before the Indian Claims Commission. Every

> effort should be made to see that this money is not dissipated on a per capita payment basis to the tribal members. The pressure from Indians living away from the reservation is often too much for tribal councils to resist, with the result that all or a substantial portion of the judgment funds are distributed to individuals. It should be emphasized to tribes that the claims awards are made to the entire group, rather than to the individual members, and the Secretary of the Interior should, except in rare cases, give first priority to group uses of the awards. If planning for resource development is carried out prior to the time the judgment is made, the hands of the tribal council and the Secretary will be considerably strengthened in resisting the pressures for per capita payments. [*Report to the Secretary of the Interior by the Task Force on Indian Affairs,* p. 13, on file at the Library of the Department of the Interior, Washington, D. C.]

With the Tribal membership asking for a per capita distribution and the Interior Department opposing such payments, the Nez Perce Tribal Executive Committee and the Department finally reached a compromise. As provided in Public Law 87-24, agreement of both parties was necessary to expend any of the funds. The compromise provided for the distribution of $750 per capita and the retention of the remainder of the funds for use in a program to improve the economic and social conditions of the Tribal membership. R. 25-26.[1] In reviewing this action the Associate Commissioner of Indian Affairs subsequently stated:

> When the governing body, in the case of the Nez Perce the Nez Perce Tribal Executive Committee, authorized a $750 per capita distribution from this fund—a de-

[1] On March 25, 1963, while the appellants' motion to dismiss was pending in the District Court, the Bureau of Indian Affairs approved an additional distribution of $500 for each member of the Tribe, subject to certain safeguards against waste. Thus, each member of the Tribe has now received $1,250 from the judgment funds at a total cost of more than $2,500,000. This is nearly half of the net amount which the Nez Perce Tribe of Idaho received under the apportionment formula in Public Law 87-24.

> cision approved by the Secretary—only that portion required to pay each enrolled member of the Nez Perce Tribe was individualized. The Nez Perce Tribal Executive Committee has stated that the balance of the funds would be used to invest in projects which will provide lasting benefits to the tribal members. To reach this goal, the Executive Committee appointed a Development Advisory Committee, which is now engaged in determining the projects best suited to improve social and economic conditions of the tribe.
>
> We fully appreciate the concern of the members of the Indian tribes living away from the reservation and hope that wherever possible they too will benefit from successful on-reservation programs. Much of our Indian population has moved to areas of greater economic opportunity throughout the entire United States and this has created different interests and different opinions as to how tribal money should be used. *It has been our experience that per capita distributions of sizeable amounts have not always produced desirable or long-lasting benefits.* [R. 24, emphasis supplied.]

The object of this suit is to prevent the Nez Perce Tribal Executive Committee from carrying out that portion of its agreement with the Department of the Interior which calls for the expenditure of funds for economic and social improvement and thus to frustrate the stated policies of the United States Government. The specific projects of which appellants complained are:

(1) a sanitation facilities program under the Indian Sanitation Act (42 U.S.C. § 2004a), financed jointly by the United States Public Health Service and the Nez Perce Tribe;

(2) the construction of two community buildings under the Public Works Acceleration Act of 1962 (76 Stat. 541), financed jointly by the Community Facilities Administration and the Nez Perce Tribe;

(3) a tourist enterprise on which the Area Redevelopment Administration has expended funds and on

which the United States Park Service and the Nez Perce Tribe may collaborate in the future.[2]

In asking the Federal courts to enjoin the expenditure of Tribal funds on projects of this nature, appellants evidently hope to obtain a distribution to all members of a "pro-rata portion" of all Tribal funds. Complaint, Section V, R. 5.

II. APPELLANTS' CONTENTIONS

In support of their request that the District Court enjoin the expenditure of Tribal funds on projects of community betterment, appellants advanced only two legal arguments. These were:

(1) that the Revised Constitution and By-Laws of the Nez Perce Tribe are "illegal and invalid" and that appellees, members of the Nez Perce Tribal Executive Committee, therefore lack authority to act as the governing body of the Tribe; (Complaint, Sections III and IV, R. 4-5);[3]

(2) that if defendants have authority to act as the Nez Perce Tribal Executive Committee, they have "exceeded the bounds of discretion" (Brief for Appellants, p. 28) in that they have failed to credit the individual accounts of plaintiffs and other Tribal members with a pro-rata portion of Tribal funds and by allegedly expending or intending to expend funds on a forestry project, a tourist enterprise, the construction of outdoor privies and the construction of community buildings (Complaint, Sections V and VIII, R. 5-6).

Appellees moved to dismiss the complaint on four separate grounds, any one of which would justify dismissal,

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[2] A forestry project referred to in the Complaint (R. 5), was considered but not put into effect.

[3] It is worthy of special note that at the time the suit was brought only defendants Gould, Thomas and Types had been elected under the 1961 Constitution. The other defendants had been elected to their positions under the 1948 Constitution.

namely: (1) failure to state a claim upon which relief can be granted; (2) lack of jurisdiction because the complaint does not state a Federal question; (3) failure to join an indispensable party, the Nez Perce Tribe; and (4) failure to join an indispensable party, the United States. The District Court granted appellees' motion.

In this brief appellees will discuss the four grounds for dismissal separately. Where appropriate, appellees will distinguish in their discussions of the applicable law between appellants' two major contentions: (1) illegality of the Tribal government, and (2) misuse of Tribal funds.

III. THE DISTRICT COURT WAS CORRECT IN DISMISSING THE COMPLAINT

A. The Complaint Fails to State a Claim Upon Which Relief Can Be Granted

(1) *The alleged illegality of the Tribal government.*

The specific grounds for the alleged invalidity of the Tribal Constitution, as set forth in Section IV of the Complaint, are:

(a) the Constitution "was adopted by a vote of 132 Tribal members out of approximately 2,000 Tribal members, far short of the required number;"[4]

(b) the Constitution denies "Indians living off the reservation the right to vote or hold office, a violation of the United States Constitution;"

(c) the Constitution "places the sole governing power in the hands of a nine-man executive committee, a denial of due process;"

(d) the Constitution "purports to give the Nez Perce Tribe powers under that certain act of Congress appearing at 48 Stat. 984, commonly known as the Wheeler-Howard Act." R. 5.

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[4] The membership total cited by appellants includes minors, who are ineligible to vote.

Before examining the law applicable to these assertions, the relevant facts and the position of the appellants should be clarified.

(a) The present Nez Perce Tribal Constitution was indeed adopted by a vote of 132 Tribal members, voting at a duly called meeting of the General Council of the Nez Perce Tribe. R. 22. This action took place under Article IX of the 1948 Constitution, which permitted amendments by "majority vote of the General Council" (Appendix A, p. 4a), and under Article II, Section 6 of the 1948 By-Laws, which provided that 50 members constitute a quorum of the General Council (*Id.*, at p. 6a).

As 132 votes were cast on the 1961 Constitution and the quorum requirement was 50, it is clear that the provisions of the 1948 By-Laws were complied with. To be meaningful, appellants' contention must, therefore, be construed as a challenge to the quorum provision of the 1948 By-Laws. Appellants are apparently asking, at this late date, that the courts rewrite the 1948 By-Laws by increasing, through judicial fiat, the quorum requirement.

It is worth noting that the Constitution of the State of Idaho provides that Constitutional amendments proposed by the Legislature shall be adopted "if a majority of the electors shall ratify the same . . ." Art. XX, Sec. 1. This language has been construed to mean that a proposed amendment is adopted if approved by a majority of the electors *who vote on that particular issue,* even if that is less than a majority of the qualified electors who vote for State officers in the same election. *Green* v. *State Board of Canvassers,* 5 Idaho 130, 47 Pac. 259 (1910). Thus, Idaho has no minimum requirement for voter participation for the adoption of a constitutional amendment.

(b) With respect to residence, the present Tribal Constitution provides in Article V, Section 5, that in order to vote at a General Council a member must have resided for the preceding six months in the Nez Perce area as established by the Treaty of 1855

(12 Stat. 957). R. 9-10. That area extends far beyond the present Reservation and encompasses such distant communities as Moscow, Idaho; Pomeroy, Washington; and Enterprise, Oregon.

The right to hold Tribal office is limited by Article VI, Section 3 to members who resided for one year in the Nez Perce Area established by the Treaty of 1863 (14 Stat. 647). R. 11.

By comparison, the Constitution of the State of Idaho provides that in order to be eligible to vote a person must be a resident of the State for 6 months preceding any election (Art. VI, § 3), and that candidates for governor, lieutenant governor, secretary, auditor, treasurer and attorney general must be residents of the State for two years preceding their election (Art. V, § 3).

What appellants seem to be seeking is a decree declaring the residence requirements of the 1961 Constitution for voting and for election to office invalid, even though they are less restrictive than the comparable provisions in the Constitution of the State of Idaho.

(c) The Revised Constitution does indeed place the authority to conduct the day-to-day Tribal business affairs in the hands of the elected Tribal Executive Committee. Article VI, Section 1, R. 10. Similar delegations of authority to elected officials are commonplace throughout our system of government, the New England town meeting constituting a rare exception.

(d) Plaintiffs were in error when they alleged that the Nez Perce Tribe purported to derive authority from the Indian Reorganization (Wheeler-Howard) Act, 48 Stat. 984 (1934). As the Court will see from an examination of the Record, the Tribal Constitution makes no reference whatever to that Act. R. 7-20. Moreover, the Associate Commissioner of Indian Affairs has stated expressly that the Nez Perce Constitution was approved by the Commissioner of Indian Affairs under the authority of 25 U.S.C. § 2. R. 23. In their

> brief before this Court, appellants appear to accept appellees' assertion that the Nez Perce Constitutions were approved by the Commissioner of Indian Affairs under the authority vested in him by 25 U.S.C. § 2. Brief for Appellants, p. 12. Since appellees now agree with appellants that the Indian Reorganization Act is inapplicable to the Nez Perce Tribe, this is not an issue in controversy in this law suit.

By challenging the validity of the Tribal Constitution, appellants are in effect, asking this Court to set aside the decisions of the Tribal membership as to their form of government and the Commissioner's approval of these decisions, and to prescribe judicial standards concerning (1) how much voter participation should be required to adopt a Tribal Constitution, (2) what are reasonable residence requirements for Tribal elections, and (3) how much authority a tribe should delegate to its officials. The District Court agreed with appellees' contention that questions of this nature are beyond the purview of the judiciary.

In framing the provisions of its Tribal Constitution the Nez Perce Tribe exercised its broad authority of self-government, which has long been recognized under our law. A landmark opinion of the Solicitor of the Department of the Interior, concerning the powers of Indian Tribes, states the underlying principle as follows:

> Since any group of men, in order to act as a group, must act through forms which give the action the character and authority of group action, an Indian tribe must, if it has any power at all, have the power to prescribe the forms through which its will may be registered. The first element of sovereignty, and the last which may survive successive statutory limitations of Indian tribal power, is the power of the tribe to determine and define its own form of government. Such power includes the right to define the powers and duties of its officials, the manner of their appointment or election, the manner of their removal, the rules they are to observe in their capacity as officials, and the

> forms and procedures which are to attest the authoritative character of acts done in the name of the tribe. [Sol. Op., Oct. 25, 1934, 55 I.D. 15, 30, reprinted in *Cohen, Handbook of Federal Indian Law* 126 (1941)]

The power of tribal self-government "also includes the power to interpret its own laws and ordinances, which interpretations will be followed by the federal courts." *Cohen, Handbook of Federal Indian Law 126* (1941).[5]

The right to define the powers of its officials and to specify the manner of their election is thus within the power of an Indian tribe. It includes the power to "classify various types of membership and qualify not only the property rights, but the voting rights of certain members." Sol. Op., Oct. 25, 1934, 55 I.D. 15, 35, citing 19 Ops. Att'y. Gen. 389 (1888). It has also been held that absent Congressional legislation or Secretarial regulations to the contrary, an Indian Tribe may adopt or amend its constitution "if a majority of those voting in the election voted in favor of its adoption, and the number of voters participating in the election would be immaterial." Sol. Op., Nov. 21, 1952, 61 I.D. 82, 85.

Appellees do not contend that the exercise of Indian self-government is not wholly free from Federal control. But they do contend that the decision of whether, and to what extent, a group of aboriginal residents of the United States is to be recognized as a self-governing body is a political question which, under our Constitution, is exclusively delegated to Congress and the Executive Branch. The Supreme Court said in the leading case of *United States* v. *Holliday,* 70 U.S. (3 Wall) 407, 419 (1866):

> The facts in the case . . . show distinctly "that the Secretary of the Interior and the Commissioner of Indian Affairs have decided that it is necessary, in

[5] Felix S. Cohen, author of the *Handbook,* has been described by the Supreme Court of the United States as "an acknowledged expert in Idnian law." *Squire* v. *Capoeman,* 351 U.S. 1, 8-9 (1956).

> order to carry into effect the provisions of said treaty, that the tribal organization should be preserved." In reference to all matters of this kind, *it is the rule of this court to follow the action of the executive and other political departments of the government,* whose more special duty it is to determine such affairs. *If by them those Indians are recognized as a tribe, this court must do the same.* If they are a tribe of Indians, then, by the Constitution of the United States they are placed, for certain purposes, within the control of the laws of Congress. [Emphasis supplied].

This principle was reaffirmed in *United States* v. *Sandoval,* 231 U.S. 28, 46 (1913). When questions have arisen as to the authority of specific individuals to act on behalf of their tribe, the Supreme Court has, applying the same rule, held that the judiciary would abide by the decision of the other branches of Government. *Fellows* v. *Blacksmith,* 60 U.S. (19 How.) 366 (1857); *United States* v. *New York Indians,* 173 U.S. 464 (1899).

Applying this rule, the lower courts have repeatedly held that internal tribal disputes cannot be resolved in Federal courts. The Court of Claims in a recent case involving rival tribal factions and two sets of attorneys, each claiming to represent the tribe, refused to decide the matter and referred the question of which attorneys properly represented the tribe to the Commissioner of Indian Affairs. *McCauley* v. *United States,* 113 F. Supp. 689 (Ct. Cl. 1953). In the recent case of *State* v. *Bertrand,* 378 P. 2d 427 (Wash. 1963) the Supreme Court of Washington refused to determine which of two rival factions had authority to speak for an Indian tribe under a Washington law which permitted Indian tribes to accept State law enforcement on their reservations. The question, said the Court, was for the political officials of the State to determine. See also *Pueblo of Santa Rosa* v. *Fall,* 273 U.S. 315 (1927) where the Supreme Court looked to internal tribal laws and custom to determine whether a purported tribal spokesman had authority to act on behalf of the tribe.

To summarize, the framing of a tribal Constitution is, in the first instance, an internal tribal affair. See generally, *Cohen, Handbook of Federal Indian Law* 126 (1941). Tribal rights of home rule can, of course, be modified by Congress. See e.g. 25 U.S.C. § 476; *Iron Crow* v. *Oglala Sioux Tribe,* 231 F. 2d 89 (8th Cir. 1956). Furthermore, Congress has vested supervisory authority over "all matters arising out of Indian relations" in the Commissioner of Indian Affairs, under the direction of the President and the Secretary of the Interior. 25 U.S.C. § 2. The Commissioner's authority under 25 U.S.C. § 2 is exceedingly broad. *Rainbow* v. *Young,* 161 Fed. 835, 838 (8th Cir. 1908); *Armstrong* v. *United States,* 306 F. 2d 520 (10th Cir. 1962). See also *Iron Crow* v. *Ogallala Sioux Tribe,* 129 F. Supp. 15, 19 (D.S.D. 1955), *aff'd.* 231 F. 2d 89 (8th Cir. 1956). The power to manage "Indian relations" must encompass the power to approve Tribal constitutions, for a principal purpose of these constitutions is to provide the framework for a continuing relationship between the Tribe and the United States. R. 23 The Commissioner and Secretary have interpreted § 2 as giving them the power to approve Tribal Constitutions (*Ibid.*) and their interpretation is entitled to "considerable weight". *Ketchikan Packing Co.* v. *Seaton,* 267 F. 2d 660, 663 (D.C. Cir. 1959).

As applied to the facts of the instant case, the foregoing rules lead to the inescapable conclusion that that portion of the complaint alleging the illegality of the Nez Perce government fails to state a claim upon which relief can be granted. This is an action to strike down the self-governing institutions of the Nez Perce people and to declare invalid the instruments by which the Executive and Legislative branches recognize the elected representatives as authoritative spokesmen for the Tribe. Appellees have shown that the quorums, residence requirements for voting and holding office, and the delegation of political power to an elected representative body, as provided for in the Nez

Perce Constitutions of 1948 and 1961, are reasonable in fact and, in any event, beyond the authority of this Court to review. Appellants can cite no case in over 175 years of United States history, in which any court attempted to substitute its judgment of what constitutes proper political institutions of an Indian tribe for that of the members of the tribe, on the one hand, or the Congress and Executive on the other. The decisions indicate, on the contrary, that Court's will invariably defer in such matters to the internal rules of the tribe itself, or to Congress and the Executive.

(2) *The alleged misuse of Tribal funds*

Assuming that the Nez Perce Tribal Executive Committee possesses the legal authority to act as the governing body of the Nez Perce Tribe, has it abused its discretion by appropriating funds for community improvement projects?

Article VI, Section 1 of the Revised Constitution states that the "affairs of the Nez Perce Tribe of Idaho shall be administered by a Tribal Executive Committee." R. 10. Article VIII, Section 1(b) grants the Committee the power "to promote and protect the health, education and general welfare of members of the Tribe." R. 13. Article VIII, Section 2, grants the Committee the power, subject to the approval of the Secretary of the Interior, "to manage the property of the Nez Perce Tribe" (subsection a), and "to engage in any business or other economic transaction that will further the economic development of the Tribe and its members" (subsection b). R. 14. Finally, Public Law 87-24 provides that the Tribe's judgment funds may "be advanced or expended for any purpose that is authorized by the [Nez Perce Tribal Executive Committee] and approved by the Secretary of the Interior." 75 Stat. 45.

A self-evident corollary of the doctrine of inherent tribal self-government previously discussed, is the principle that

tribal laws enacted in the exercise of the tribe's powers of self-government are beyond the purview of judicial review. This rule was clearly laid down by the Supreme Court in *Talton* v. *Mayes,* 163 U.S. 376 (1896) and has been recently reaffirmed in *Barta* v. *Oglala Sioux Tribe,* 259 F. 2d 553 (8th Cir. 1958), *cert. den.,* 358 U.S. 932 (1959); *Native American Church* v. *Navajo Tribal Council,* 272 F. 2d 131 (10th Cir. 1959); *Oliver* v. *Udall,* 306 F. 2d 819 (D.C. Cir. 1962), *cert. den.* 372 U.S. 908 (1963). The doctrine is so far-reaching that even the actions of tribal governments which allegedly violate the Constitution of the United States are said to be beyond the scope of judicial review. *Talton* v. *Mayes, supra; Native American Church* v. *Navajo Tribal Council, supra.*

Appellants have cited no legal authority for the proposition that the fact that an Indian governing body has expended or plans to expend funds on community improvement projects gives rise to a judicially cognizable claim. See *Massachusetts* v. *Mellon,* 262 U.S. 447 (1926). On the contrary, where, as here, the law has granted approval powers to the Secretary of the Interior, it is clear that supervisory authority is to be exercised by the Executive and not by the Judiciary. *Prairie Band of Pottawatomie Indians* v. *Puckkee,* 321 F. 2d 767 (10th Cir. 1963).

B. The District Court Lacked Jurisdiction Over the Subject Matter

1. *General rules of jurisdiction apply.*

The Federal courts are, of course, courts of limited jurisdiction and can take cognizance only of those matters which Congress has entrusted to them by statute. There is no statute giving Federal courts jurisdiction over all causes of action involving Indians or Indian tribes, or simply because the contracts or property of an Indian tribe are involved. *Martinez* v. *Southern Ute Tribe,* 249 F. 2d 915, 917 (10th Cir. 1957), *cert. den.* 356 U.S. 960 (1958). Hence, the jurisdiction of this Court must depend upon generally applicable rules of Federal jurisdiction.

Since the complaint states that "all parties hereto . . . reside in the above entitled Judicial District" (R. 4), diversity of citizenship does not exist. The only other possibility for Federal jurisdiction is the existence of a Federal question; that is, a controversy which "arises under the Constitution, laws or treaties of the United States." 28 U.S.C. § 1331. See *Gustason* v. *California Trust Co.,* 73 F. 2d 765 (9th Cir. 1934), *cert. den.* 296 U.S. 607 (1935).

2. *The complaint does not raise a Federal question.*

The existence of a federal question must be found in the well-pleaded allegations of the complaint. *Skelly Oil Co.* v. *Phillips Petroleum Co.,* 339 U.S. 667, 673 (1950). A cause of action does not "arise under the Constitution, laws or treaties of the United States" unless "the complaint is drawn . . . so as to claim *a right to recover* under the Constitution and laws of the United States." *Bell* v. *Hood,* 327 U.S. 678, 680 (1946) (emphasis supplied). It is not sufficient merely to allege some vague, undefined Federal right. The right claimed must "clearly appear." *Consolidated Freightways* v. *United States Truck Lines,* 216 F. 2d 543 (9th Cir. 1954), *cert. den.* 349 U.S. 905 (1955). "To bring a case within the statute [28 U.S.C. § 1331], a right or immunity created by the Constitution of the United States must be an element, *and an essential one,* of plaintiff's cause of action." *Gully* v. *First National Bank,* 299 U.S. 109, 112 (1936) (emphasis supplied).

By these tests, it clearly appears that no Federal question is presented in this action. While the complaint makes vague reference to "the laws and Constitution of the United States Government" (R. 4), no specific portion of the Constitution is cited, and no claim of right or immunity created by any law or the Constitution is clearly asserted.

Appellants purport to derive some comfort from the fact that *appellees,* in support of their motion to dismiss, relied upon two Federal statutes, namely 25 U.S.C. § 2,

and Public Law 87-24. Brief for Appellants, p. 11. But federal-question jurisdiction depends upon the allegations of a well pleaded complaint. Jurisdiction cannot be conferred by the defendant's answer, much less by a memorandum in support of a motion to dismiss. Nor can the plaintiff obtain federal-question jurisdiction by anticipating in its complaint an affirmative defense that might bring Federal law into issue. *Skelly Oil Co.* v. *Phillips Petroleum Co., supra.*

3. *The complaint could not raise a Federal question.*

What is perhaps equally important is the fact that under the existing legal rules governing judicial supervision of the internal affairs of an Indian tribe, no claim "arising under the Constitution or laws of the United States" could be here asserted.

The judgments of the Indian Claims Commission were rendered in favor of the Nez Perce Tribe, and not its individual members. *Nez Perce Tribe* v. *United States,* 8 Ind. Cl. Com. 759 (1960); *Nez Perce Tribe* v. *United States,* 8 Ind. Cl. Com. 300 (1959). The funds authorized by those judgments, like the land which they represent, is held in common by the Tribe. Appellees' repeated assertions to the contrary notwithstanding (e.g., Brief for Apellant, p. 18), no individual tribal member has an individualized, vested right in communal tribal property. *Minnesota Chippewa Tribe* v. *United States,* 315 F. 2d 906, 913-14 (Ct. Cl. 1963); *Cohen, Handbook of Federal Indian Law* 183-84 (1941). See letter of Associate Commissioner, R. 23.

In this situation it is perfectly clear that no Federal question is presented. The right to use and dispose of tribal property remains solely in the Tribe, except as limited by Congress. Our courts have clearly and repeatedly "declined to interfere with the decisions of tribal authori-

ties on property disputes internal to the tribe." *Federal Indian Law* 443 (1956), a U. S. Department of the Interior revision of Felix S. Cohen's *Handbook of Federal Indian Law,* citing cases. Disputes arising out of the use and distribution of tribal property must be resolved by tribal law and custom. In short, the issue presented arises under the laws and Constitution of the Nez Perce Tribe, and not the laws, treaties or Constitution of the United States.

Three recent decisions will conclusively establish the proposition that no Federal question is here involved:

a. The recent case of *Prairie Band of Pottawatomie Tribe* v. *Puckkee,* 321 F. 2d 767 (10th Cir. 1963) is virtually identical to the instant action. There certain members of the Tribe brought suit against other named members of the Tribe to declare plaintiff's rights in certain tribal judgment funds, which had been entrusted to tribal control under statutory language identical with that involved in the instant case. See Act of September 6, 1961, 75 Stat. 474. The Court held no Federal question was presented.

b. In *Washburn* v. *Parker,* 7 F. Supp. 120 (W.D. N.Y. 1934) an action was brought to restrain a tribal court of the Seneca Nation from resolving a dispute between two tribal members concerning the partition of certain real estate. The Court refused to entertain the action on the grounds that "in the absence of congressional action bestowing upon the individual Indians the right to litigate internal questions relating to their property rights in the federal courts, and conferring jurisdiction upon this court to determine such controversies, this court should not assume jurisdiction," *Ibid.,* quoting *United States* v. *Seneca Nation,* 274 Fed. 946, 951 (W.D. N.Y. 1921).

c. In a pair of cases, strikingly similar to the instant case, an alleged member of the Southern Ute Tribe in Utah sued the Tribe and the members of its governing body to enforce her claim that she was entitled to participate in a per capita distribution by the Tribe. *Martinez*

v. *Southern Ute Tribe,* 249 F. 2d 915 (10th Cir. 1957), *cert. den.* 356 U.S. 960 (1958); *Martinez* v. *Southern Ute Tribe,* 273 F. 2d 731 (10th Cir. 1960), *cert. den.* 363 U.S. 847 (1960). The Tenth Circuit twice held that the complaints did not state a cause of action arising under the Constitution, laws or treaties of the United States and dismissed the suits for lack of jurisdiction over the subject matter.

The foregoing cases conclusively demonstrate that the allegations of abuse of discretion and misuse of tribal funds in the appellants' complaint raise no issues arising under the laws of the United States. Public Law 87-24 directs that the Nez Perce judgment funds may be "advanced or expended for any purpose that is authorized by the respective tribal governing bodies and *approved by the Secretary of the Interior.*" 75 Stat. 45 (emphasis supplied). Precisely the same provision was contained in the statutes involved in the *Ute* and *Pottawattomie* cases. See *Martinez* v. *Southern Ute Tribe,* 273 F. 2d at 733; *Prairie Band of Pottawattomie Tribe* v. *Puckkee,* 321 F. 2d at 769.

While *Congress* has undoubted authority to intervene in the internal affairs of Indian tribes, it has long been clear to our courts that "Congress at no time intended to provide for federal supervision of private civil actions by Indians." *Martinez* v. *Southern Ute Tribe,* 249 F. 2d at 919. This is an "intra-tribal controversy, over which Federal court jurisdiction has been traditionally denied." *Prairie Band of Pottawatomie Tribe* v. *Puckkee,* 321 F. 2d at 770 (10th Cir. 1963). See also *Native American Church* v. *Navajo Tribal Council,* 272 F. 2d 131 (10th Cir. 1959); *Talton* v. *Mayes,* 163 U.S. 376 (1896).

In their brief appellants have cited a number of cases which they claim establish the proposition that courts have accepted jurisdiction over causes of action involving Indian funds and property. Brief for Appellants, p. 13. This

is undeniably true. But each of the cases cited by appellants was either brought by an Indian tribe and raised a Federal question on the face of the complaint or was brought pursuant to a special jurisdictional Act of Congress. The cases cited by appellants are distinguished in the margin.[6]

The conclusion is inescapable that the complaint fails to raise a Federal question and must therefore be dismissed for lack of jurisdiction.

C. The Complaint Fails to Join An Indispensable Party—the Nez Perce Tribe

This suit is, in law as well as in fact, an action against the Nez Perce Tribe. The nine individuals named in the complaint were, as the complaint alleges, the nine members of the Nez Perce Tribal Executive Committee.

They are, as examination of the complaint demonstrates, sued in their official capacity for their official acts. More-

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[6] In *Oglala Sioux Tribe* v. *Barta,* 146 F. Supp. 917 (D.S.D. 1956), *aff'd.* 259 F. 2d 553 (8th Cir. 1958), *cert. den.* 358 U.S. 932 (1959), the Federal question arose from the fact that the tribe was suing under a tribal constitution which had been authorized by Act of Congress to collect a tax levied pursuant to that constitution. No comparable circumstances exist here.

Skokomish Indian Tribe v. *France,* 269 F. 2d 555 (9th Cir. 1959) was an action to quiet title brought by the tribe to enforce certain rights under a treaty with the United States. The Federal question was self-evident.

Sakezzie v. *Utah Indian Affairs Commission,* 198 F. Supp. 218 (D. Utah 1961), *modified* 215 F. Supp. 12 (D. Utah 1963), was an action by a group of individual Indians living in Utah to enforce their rights under an Act of Congress which obligated the State of Utah to expend certain oil royalties for the use and benefit of the plaintiffs. Act of March 1, 1933, 47 Stat. 1418. The case clearly arose under a law of the United States.

Healing v. *Jones,* 174 F. Supp. 211 (D. Ariz. 1959), *cert. den.* 373 U.S. 758 (1953) was brought under a special Act of Congress, expressly authorizing a land dispute between the Navajo and Hopi Tribes to be tried before a three judge court and conferring jurisdiction on the court to entertain the action. Act of July 22, 1958, 72 Stat. 402.

United States v. *Pierce,* 235 F. 2d 885 (9th Cir. 1956), was an action to compel the United States to issue trust patents to certain lands the plaintiffs had selected as allotments. Jurisdiction was based upon 25 U.S.C. § 345, which expressly authorizes such actions.

over, the relief requested demonstrates that the Tribe is the real subject of this suit. Any decree entered by this Court would so directly affect the Nez Perce Tribe that it "would be wholly inconsistent with equity and good conscience" to hold a trial without joining the Tribe as a party. *Shields* v. *Barrow,* 58 U.S. (17 How.) 130, 139 (1855).

The tests of whether a party is indispensable have been stated by the Supreme Court as follows:

> Persons who not only have an interest in the controversy, but an interest of such a nature that a final decree cannot be made without either affecting that interest, or leaving the controversy in such a condition that its final termination may be wholly inconsistent with equity and good conscience [are indispensable parties]. [*Shields* v. *Barrow,* 58 U.S. (17 How.) 130, 139 (1855)].

In another case the Supreme Court stated that a party is indispensable if:

> [t]he court would find itself in the position of having made a decree it could not enforce, of attempting to give relief which is beyond its power, because the party whose action was necessary to that relief was not a party to the suit. [*Kendig* v. *Dean,* 97 U.S. 423, 424 (1878)].

See generally, 3 *Moore, Federal Practice* 2150 (1963).

This principle was expressly applied in *Barnes* v. *United States,* 205 F. Supp. 97 (D. Mont. 1962), where a member of the Crow Indian Tribe sued the Chairman of the Tribe, the Commissioner of Indian Affairs, the Secretary of the Interior and others to annul and set aside a resolution of the Crow Tribal Council and enjoin the defendants from carrying out the resolution. That case, too, concerned the use and distribution of tribal funds.

The District Court granted defendant's motion to dismiss on the ground, *inter alia,* that the Crow Tribe was an

indispensable party over which the Court lacked jurisdiction. The Court, in a scholarly opinion, stated:

> An Indian tribe is not subject to suit without the consent of Congress. *Nor may a tribe be sued indirectly by suing its tribal officers* or the United States as trustee or guardian of the tribe. No law has been cited and none can be found which would subject the Crow Tribe to a suit of the nature involved in this action. [205 F. Supp. at 100 (emphasis supplied)].
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> * * *
>
> . . . *the Crow tribe may not be sued indirectly by suing a tribal officer.* [205 F. Supp. at 101]

See also *Thebo* v. *Choctaw Tribe,* 66 Fed. 372 (8th Cir. 1895); *Adams* v. *Murphy,* 165 Fed. 304 (8th Cir. 1908). Compare, *Tower Hill Connellsville Coke Co.* v. *Piedmont Coal Co.,* 33 F. 2d 703, *rehearing den.* 35 F. 2d. 179 (4th Cir. 1929), *cert. den.* 260 U.S. 607 (1930); (in suit against corporate directors to compel payment of dividends the corporation is an indispensable party); *Gray* v. *Reuther,* 99 F. Supp. 992 (E.D. Mich. 1951), *aff'd per curiam* 201 F. 2d 54 (6th Cir. 1952) (in suit against individual union officers for an accounting of their control of local union funds the local union is an indispensable party); *Hanson* v. *Hutcheson,* 217 F. 2d 171 (7th Cir. 1954) (same); *Green* v. *Brophy,* 110 F. 2d 539 (D.C. Cir. 1940).[7]

The law is clear beyond dispute that if an indispensable party cannot be joined, the suit must be dismissed. *Shields* v. *Barrow, supra; Hanson* v. *Hutcheson, supra; Gray* v. *Reuther, supra.* See generally, 3 *Moore, Federal Practice,*

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[7] None of the cases cited by appellants is in the remotest way relevant to the question of whether the Nez Perce Tribe is an indispensable party defendant. *Sakazzie* v. *Utah Indian Affairs Commission,* 198 F. Supp. 218 (D. Utah 1961), *modified* 215 F. Supp. 12 (D. Utah 1963) was a suit by individual Indians to enforce their rights against a governmental commission created by the State of Utah. No Indian tribe was involved. In *Choctaw and Chickasaw Nations* v. *Seitz,* 193 F. 2d 456 (10th Cir. 1951), *cert. den.* 343 U.S. 919 (1952), and *Lane* v. *Pueblo of Santa Rosa,* 249 U.S. 110 (1919) the Tribe was the party plaintiff, hence no question as to its indispensability was raised.

2205 (1963). Defendants submit that this is the inescapable result in this case.

The indispensable party—the Nez Perce Tribe of Idaho —is not subject to suit in the Federal Courts. In a recent case, the Fourth Circuit succinctly stated the law on this question:

> The rule that a tribe of Indians under the tutelage of the United States is not subject to suit without the consent of Congress is too well settled to admit of argument. [*Haile* v. *Saunooke,* 246 F. 2d 293, 297 (4th Cir.) *cert den. sub. nom. Haile* v. *Eastern Band of Cherokee Indians,* 355 U.S. 893 (1957)].

The court relied upon such cases as *Thebo* v. *Choctaw Tribe,* 66 Fed. 372 (8th Cir. 1895), and *United States* v. *United States Fidelity & Guarantee Co.,* 309 U.S. 506, 512 (1940), wherein the Supreme Court stated "[t]hese Indian nations are exempt from suit without Congressional authorization." There is no Act of Congress authorizing suits such as the instant one against an Indian tribe. See *Cohen, Handbook of Federal Indian Law* 283 (1941). Since the Nez Perce Tribe is an indispensable party and since the Tribe cannot be sued and joined, the case must be dismissed.

D. The Complaint Fails to Join An Indispensable Party—the United States

Each of the principal allegations of the complaint, the illegality of the Nez Perce Tribal Government and the misuse of tribal funds, so affects the vital interests of the United States that it must be joined as a party if the suit is to proceed. Since the United States cannot be joined, dismissal of the action was required. The interest of the United States as to each of appellants' principal allegations, will be examined separately.

1. *Alleged illegality of the Tribal government.*

Since 1832, Congress has vested in the Commissioner of Indian Affairs the power of "management of all Indian

affairs and of all matters arising out of Indian relations." 4 Stat. 564, now codified as 25 U.S.C. § 2. In 1950, Reorg. Plan No. 3, §§ 1, 2, 64 Stat. 1262, transferred this power to the Secretary of the Interior. It is in the exercise of this statutory power and responsibility that the Department of the Interior approved and authorized the scheme of government for the Nez Perce Tribe set forth in the Revised Constitution of the Nez Perce Tribe. R. 23. If the District Court had considered the merits of appellants' case, it would have reviewed the actions of the Department of the Interior. If it had ruled the Tribal Constitution invalid, it would have stricken down a document which was not only approved by the Department of the Interior, but which defines the relationship of the Department to the Nez Perce Tribe. The Revised Nez Perce Constitution constitutes the working agreement between the Tribe and the United States concerning the manner in which the affairs of the Nez Perce Tribe shall be managed. If that working agreement is to be suspended or revoked, it seems clear a final decree could not be made without directly affecting the interest of the United States, and that it would be "wholly inconsistent with equity and good conscience" to hold a trial without joining the United States as a party. *Shields* v. *Barrow,* 58 U.S. (17 How.) 130, 139 (1855).

2. *The alleged misuse of Tribal funds.*

Appellants' second major contention is that even if appellees properly constitute the Nez Perce Tribal Executive Committee, their action in expending funds on community improvement programs is improper and should have been enjoined by the District Court. It is submitted that with regard to this allegation, too, the United States is an indispensable party.

As has been pointed out previously, the funds in question belong to the Nez Perce Tribe, and not to its individual members. Just as stockholders in a corporation have no

direct interest in corporate profits until a dividend is declared, members of the Tribe have no direct interest in Tribal funds. The matter has been succinctly stated by the Associate Commissioner of Indian Affairs:

> Many Nez Perce Indians, especially those living away from the reservation are of the opinion that the recent judgment awarded the Nez Perce Tribe gives each individual a "legal share". Neither the order of judgment nor the subsequent legislation (Act of April 24, 1961, 75 Stat. 45), provided for individualizing the total judgment awarded. The interlocutory order of judgment entered on December 31, 1959 found that the petitioners were entitled to recover on behalf of the *Nez Perce Tribe.* The Act of April 24, 1961, *supra* provided that these funds may be used or expended for any purpose authorized by the tribal governing body and approved by the Secretary of the Interior. [R. 23-24].

The Secretary of the Interior, when approving the initial per capita payment of $750, stated "we anticipate that the Tribe will be able to use the balance of its available funds for development programs that will be of lasting benefit to the Tribe and its members." R. 25. He added, "with the bulk of the money to be programmed for the productive and enduring benefit of the Tribe and its members, we can anticipate better times ahead for the Nez Perce Indians." R. 26.

To enjoin the expenditure of these funds for development programs that have been encouraged and approved by the Secretary, pursuant to his authority under Public Law 87-24, would surely be to affect the vital interests of the United States.

The Supreme Court faced a wholly comparable problem in *Morrison* v. *Work,* 266 U.S. 481 (1925). There a class suit was brought on behalf of all Chippewa Indians against the Secretary of the Interior and other Government officials. The suit charged that the defendants had failed to make

certain per capita distributions of tribal trust funds, as required by a special law pertaining to the Chippewas. The Court found that the suit which sought "to interfere with its [the United States'] management and disposition of the lands or the funds by enjoining its officials would interfere with the performance of governmental functions and vitally affect the interests of the United States." *Id.* at 486. The Court consequently held the United States to be an indispensable party to the suit, and affirmed dismissal of the case on the ground that the United States had not consented to be sued. To the same effect is *First National Bank of Holdenville, Okla.* v. *Ickes,* 60 F. Supp. 366 (D. D.C. 1945), *aff'd* 154 F.2d 851 (D.C. Cir. 1946).

In the recent Crow case discussed above, *Barnes* v. *United States,* 205 F. Supp. 97 (D. Mont. 1962), the court addressed itself to this specific problem and pointed out that the Crow judgment fund could not be expended except upon approval of the Secretary of the Interior. The court then pointed out:

> Any decree which might be entered would require the Secretary to take action or refrain from taking action, "either by exercising directly a power lodged in him or by having a subordinate exercise it for him." It is well settled that in such a case the superior officer, here the Secretary of the Interior, is an indispensable party. [205 F. Supp. at 101]

Precisely the same situation exists in the instant case. See Pub. L. 87-24, 75 Stat. 45.

To restrain the expenditure of all tribal funds, as appellants request, would:

1. Cut off the expenditure of the tribal judgment funds and thus prevent the Tribe from accomplishing the development goals which the Secretary has described as an outstanding opportunity to provide "for the productive and enduring benefit of the tribe and its members." R. 26.

2. Prohibit the expenditure of all other tribal funds, including tribal trust funds, which are under the control of the Secretary of the Interior.
3. Preclude tribal expenditures to provide educational assistance and scholarships to tribal members.
4. Preclude expenditures to provide welfare assistance to needy tribal members.
5. Prevent expenditures to provide for the maintenance, protection and development of tribal property and resources.

It is self-evident that the frustration of the foregoing would substantially thwart the programs of the United States to advance the economic and social conditions of the Nez Perce Tribe.

Since the United States is for the foregoing reasons an indispensable party and since it has not consented to be sued in a case such as the instant one, the complaint must be dismissed.[8] See authorities cited in Section III, C of this Brief, *supra.*

CONCLUSION

In their lengthy conclusion appellants have suggested that if they are deprived of the opportunity to litigate the merits of this complaint, such a result would be a consequence of their status as Indians. This is most certainly not the case. The fact of the matter is that the relief which they seek, judicial revision of the Constitution and By-laws of the Nez Perce Tribe and judicial division per capita of Tribal assets, would not be available to them if they were non-Indians seeking such relief against their local government or even against the directors of a voluntary associa-

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[8] The cases cited by plaintiff appear to be wholly inapplicable. *Choctaw and Chickasaw Nations* v. *Seitz,* 193 F. 2d 456 (10th Cir. 1951), *cert. den.* 343 U.S. 919 (1952), was an action by the tribes to establish title to certain lands. The Court, relying upon well established precedent, held that a tribe could sue to recover lands without joining the United States as a party.

tion. As it is, individual tribal members are protected against abuse of discretion by the tribal leadership by the supervisory authority of the Secretary of the Interior.

For the foregoing reasons the decision of the District Court should be affirmed.

Respectfully submitted,

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CERTIFICATE

I certify that in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

_____

Counsel for Defendant-Appellees

APPENDIX

APPENDIX A

1948 Constitution and By-Laws of the Nez Perce Tribe In Idaho

Preamble

We, the members of the Nez Perce Tribe in Idaho, in order to exercise our tribal rights and promote our common welfare do hereby ordain and establish this Constitution and By-Laws.

Article I—Purpose

The purpose shall be to protect and promote the interests of the Nez Perce Indians, to develop cooperative relations with the Office of Indian Affairs, and to cooperate with State and local governments.

Article II—Name

This tribal organization shall be called "The Nez Perce Tribe".

Article III—Territory

The jurisdiction of the Nez Perce Tribe shall extend to all lands within the original confines of the Nez Perce Reservation boundaries as established by treaty; and to such other lands as may hereafter be acquired by or for the Nez Perce Indians of Idaho.

Article IV—Membership

Section 1. The membership of the Nez Perce Tribe shall consist as follows, of:

(a) All persons of Nez Perce Indian blood whose names appear on the official census roll of the Nez Perce Tribe as of July 1, 1940; provided, that corrections may be made in the said roll by the Tribal Executive Committee within five years from the adoption and approval of this Constitution, subject to the approval of the Secretary of the Interior or his authorized representative.

(b) All children, born to members of the Nez Perce Tribe, who are of at least one-fourth degree Nez Perce Indian blood.

Section 2. The Executive Committee of the Tribe shall have power to make rules, subject to approval by the Secretary of the Interior or his authorized representatives, governing the adoption of new members or the termination of membership in the Tribe.

Article V—Governing Body

Section 1. The governing body of the Tribe shall be a Tribal Executive Committee consisting of (9) nine members elected by the General Tribal Council.

Section 2. The Executive Committee shall meet immediately following the General Council each year for the purpose of electing from its own membership: (a) a Chairman, (b) a Vice-Chairman, (c) a Secretary, (d) a Treasurer, (e) an Assistant Secretary-Treasurer, and (f) a Chaplain.

Article VI—Nominations and Elections

Section 1. The election of Tribal Executive Committeemen each year shall be supervised by the Chairman, Secretary and Teller selected by the General Council.

Section 2. The present Tribal Business Committee shall continue as the governing body until a new Tribal Executive Committee shall have been elected and installed in office under this Constitution.

Section 3. In the election of Committeemen by the General Council the three nominees receiving the highest number of votes shall hold office for three (3) years, the three nominees with the next highest number of votes shall hold office for two (2) years, the three nominees with the next highest number of votes shall hold office for one (1) year. Thereafter elections for the Tribal Executive Committee

shall be held every year and such members elected shall serve for a term of three (3) years, or until their successors are duly elected.

Section 4. All elections shall be held in accordance with instructions and rules laid down by the Tribal Executive Committee.

Section 5. Any enrolled member of the Nez Perce Tribe who is twenty-one (21) years of age or over and has had a permanent residence on the Reservation for at least one year immediately preceding an election shall be entitled to vote in said election.

Section 6. The General Council officers at an election of Committeemen shall certify as to the results of said election and the eligibility of electees.

Article VII—Vacancies and Removal from Office

Section 1. Should a vacancy occur in the Tribal Executive Committee either by death, resignation or removal, the Tribal Executive Committee shall declare the position vacant and appoint a successor to serve until the next regular election.

Section 2. Any member or officer of the Tribal Executive Committee may be removed from office if convicted of any felony, or upon absenting himself from three (3) successive meetings without sufficient reason acceptable to the Committee. Removal of such member or members of the Tribal Executive Committee shall be by a majority vote of the Committee.

Section 3. The Tribal Executive Committee may, by a majority vote, expel any member for neglect of duty or gross misconduct. Before any vote for expulsion is taken in the matter, such member or officer shall be given a written statement of the charges against him at least five (5) days before the meeting of the Tribal Executive Committee before he is to appear, and he shall be given an oppor-

tunity to answer charges at the designated Committee meeting where the decision of the said committee shall be final.

Article VIII—Powers and Duties of the Tribal Executive Committee

The Tribal Executive Committee shall have the following powers subject to any limitations imposed by the Statutes or the Constitution of the United States:

(a) To represent the Tribe and to negotiate with Federal, State and local governments and to advise with representatives of the Interior Department on appropriations, projects and legislation that affect the Tribe.

(b) To manage all affairs of the Nez Perce Tribe, including the administration of Tribal lands, funds, timber and other resources, under appropriate contracts, leases, permits, and loan or sale agreements.

(c) To promulgate and enforce ordinances governing the conduct of members of the Tribe and providing for the procedures of the Tribal Executive Committee.

(d) To exercise any rights and powers heretofore vested in the Nez Perce Tribe but not expressly referred to in this Constitution, or any powers that may in the future be delegated by any agency of local, State or Federal government.

Article IX—Amendments

This Constitution and By-Laws may be amended by a majority vote of the qualified voters of the Tribe at an election called for that purpose by resolution of the Executive Committee or majority vote of the General Council, such amendments to become effective when approved by the Commissioner of Indian Affairs or his duly authorized representative.

By-Laws of the Nez Perce Tribe

Article I—Duties of the Officers

Section 1. The Chairman as chief executive officer of the Executive Committee and the Tribe, shall preside over all meetings of the Executive Committee and the General Council, affix his signature to official documents, countersign warrants duly drawn by the Treasurer against the tribal funds and shall vote only in case of a tie.

Section 2. The Vice-Chairman shall preside at meetings and otherwise act in full capacity of the Chairman in the absence of the Chairman.

Section 3. The Secretary shall conduct all correspondence, issue public notices, take minutes, record official actions, etc., of the Executive Committee and the General Council and affix his signature to official documents.

Section 4. The Treasurer shall accept, receipt for and safeguard all funds of the Tribe under his custody as directed by the Executive Committee, and keep complete record of receipts and expenditures. He shall be a bonded officer and shall not disburse any funds of the Tribe except as duly authorized by the Executive Committee and he shall report on his accounts and all financial transactions at meeting upon request of the General Council or the Executive Committee.

Section 5. The Assistant Secretary-Treasurer shall assist, or serve in the absence of either the Secretary or the Treasurer.

Section 6. The duties and compensation of all appointive committees and officers of the Tribe shall be defined by resolution or motion of the Executive Committee.

Article II—Meetings

Section 1. The Executive Committee shall meet in regular session on second Tuesday of each month.

Section 2. Special meetings of the Executive Committee may be called by the Chairman, or upon written request of at least five members of the Executive Committee.

Section 3. At any meeting of the Executive Committee duly called, five members shall constitute a quorum.

Section 4. At all meetings of the General Council or the Executive Committee, Robert's Rules of Order shall govern.

Section 5. The Tribal Executive Committee shall set dates of the General Council meetings each year.

Section 6. At meetings of the General Council, fifty (50) members present shall constitute a quorum.

Article III—Ratification

Section 1. This Constitution and By-Laws shall become effective upon ratification by a majority vote of those adult members of the Nez Perce Tribe, who shall vote in General Council assembled as authorized by the Commissioner of Indian Affairs.

Section 2. This Constitution and By-Laws are herewith approved by the Assistant Commissioner of Indian Affairs and submitted for ratification by the adult members of the Nez Perce Tribe, State of Idaho, in general assembly.

Signed: JOHN H. PROVINSE
Assistant Commissioner of
Indian Affairs

April 2, 1948
Washington, D. C.

Certification of Adoption

Pursuant to an order, approved April 2, 1948, by the Assistant Commissioner of Indian Affairs, the attached Constitution and By-Laws was submitted for ratification to the adult members of the Nez Perce Tribe in general assembly, and was on April 30, 1948, duly ratified by a vote of 93 for and 77 against.

Sgd. Sam Slickpoo
Chairman, General Council

Sgd. Allen Moody
Secretary, General Council

Sgd. Frank Raibou
Teller, General Council

Sgd. Richard A. Halfmoon
Election Judge

Sgd. Lillian Smith
Election Judge

Sgd. Archie Phinney
Supt., Northern Idaho Agency

No. 18,834

In the United States Court of Appeals for the Ninth Circuit

JESS GREEN, APPELLANT

v.

ANGUS A. WILSON, ET AL., APPELLEES

Appeal from the United States District Court for the District of Idaho

BRIEF FOR THE UNITED STATES AS *AMICUS CURIAE*

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BRIEF FOR THE UNITED STATES AS *AMICUS CURIAE*

I

INTEREST OF THE UNITED STATES

A detailed statement of the interest of the United States is contained in the Representation of Interest filed in the district court (R. 27-38). The Nez Perce Tribe has recovered $7,157,605 in judgments against the United States under the Indian Claims Commission Act, 60 Stat. 1049, 25 U.S.C. secs. 70 *et seq.* Congress has appropriated this sum, by the Act of April 24, 1961, Pub. L. 87-24, 75 Stat. 45, to be:

advanced or expended for any purpose that is authorized by the respective tribal governing bodies and approved by the Secretary of the Interior.

By this suit against the members of the tribal governing body (R. 28), appellant attacks the entire governmental system of the tribe as recognized and approved by the United States (R. 27-28) and attacks numerous specific expenditures made or contemplated by the tribal governing body. The expenditures specifically attacked include (1) the tribal sanitation facilities program (R. 2, par. V); (2) the development of tribal tourist enterprises (R. 2, par. V); and (3) the construction of tribal community centers (R. 2, par. VIII).[1] Each of the named projects, and numerous others that are dependent upon this tribal judgment fund, have been developed in cooperation with the Secretary of the Interior or his delegated representatives and have his tentative or final approval as required by the appropriation statute (R. 30-32). Appellant also requests an injunction against expenditure of any tribal funds by the tribal government (R. 3, par. IX (3)). The ultimate aim of the suit is to compel a per capita distribution of the entire judgment fund, in opposition to the uses now planned and contrary to the direction of Congress (R. 1, 2, pars. II, V).

The United States has a general interest in this suit because of its historic relationship with the tribe and as trustee of tribal funds. It has a specific inter-

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[1] A forest project under consideration was also attacked (R. 5, par. V), but it has not been put into effect.

est because (1) the attack is on the only tribal government it recognizes; (2) the attack is on expenditures it has tentatively or finally approved; (3) the requested injunction would prevent it from making any tribal expenditures (whether or not from the judgment fund) that require concurrence with the tribal government; (4) an order for per capita distribution of the judgment fund would abrogate the congressional prohibition against expenditure of any of the tribal funds without approval of the Secretary of the Interior; and (5) court intervention would, in effect, confer on the courts the supervisory jurisdiction of the Secretary of the Interior over Indian affairs.

II

DISMISSAL OF THE SUIT WAS PROPER BECAUSE OF THE ABSENCE OF THE UNITED STATES, WHICH IS AN INDISPENSABLE PARTY

Essential to any meaningful relief for appellant are findings that the tribal government recognized by the United States is illegal,[2] that the expenditures ap-

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[2] To the extent that this suit attempts to attack the governmental organization of the tribe, it must fail because of the tribe's sovereign immunity from suit. *United States* v. *U.S. Fidelity Co.*, 309 U.S. 506, 512 (1940) (appellant relies upon the court of appeals' opinion that was reversed, Br. 29); *Turner* v. *United States*, 248 U.S. 354, 358-359 (1919); *Haile* v. *Saunooke*, 246 F.2d 293, 297 (C.A. 4, 1957), cert. den., 355 U.S. 893, and cases there cited. And the tribe may not be sued indirectly by naming only the officers, since the attack obviously is upon the officers' official authority and official action. *Barnes* v. *United States*, 205 F.Supp. 97, 100 (D. Mont. 1962), and cases there cited.

proved by the United States are illegal, that issuance of the injunction freezing tribal funds held by the United States is justified, and that appellant is entitled to a vested per capita share of the judgment fund. Because of the inescapable involvement of the United States in all of these matters, we submit that the United States is an indispensable party to this suit and cannot be joined because of the absence of consent.

The classic definition of indispensable parties is stated by the Supreme Court in *Shields* v. *Barrow*, 17 How. 130, 139 (1854):

> Persons who not only have an interest in the controversy, but an interest of such a nature that a final decree cannot be made without either affecting that interest, or leaving the controversy in such a condition that its final termination may be wholly inconsistent with equity and good conscience.

This court traced the history of this definition in some detail in *State of Washington* v. *United States*, 87 F.2d 421, 425-428 (1936), and then set forth the following test for determining when a party is indispensable (pp. 427-428):

> * * * After first determining that such party is interested in the controversy, the court must make a determination of the following questions applied to the particular case: (1) Is the interest of the absent party distinct and severable? (2) In the absence of such party, can the court render justice between the parties before it? (3) Will the decree made, in the absence of such party, have no injurious effect on the interest of

> such absent party? (4) Will the final determination, in the absence of such party, be consistent with equity and good conscience?
>
> If, after the court determines that an absent party is interested in the controversy, it finds that all of the four questions outlined above are answered in the affirmative with respect to the absent party's interest, then such absent party is a necessary party. However, if any one of the four questions is answered in the negative, then the absent party is indispensable.

Asking these questions about the interest of the United States, we find that at least the first and third questions must be answered in the negative.

If it were possible for appellant to overcome the tribe's sovereign immunity (*supra*, fn. 2), the attack upon the governmental organization is a challenge of the United States' action in recognizing the tribal government and is an attempt to void that action. It is impossible to separate the interest of the United States from the interest of the tribal government in this respect. If successful, the suit would destroy the only group with which the United States can deal in supervising the many aspects of tribal life for which it is responsible.

The attack upon the proposed and actual tribal expenditures is an attack upon the cooperative action of the United States and the tribal government; the interests of the two are not severable. The tribal fund is administered cooperatively and establishment of the invalidity of the expenditures necessarily requires a finding of the invalidity of the cooperative action. This would obviously have an injurious effect upon the ab-

sent party because it would invalidate its action without its presence.[3]

The question of the indispensability of the United States has arisen in a number of cases specifically concerned with tribal property and, even without the foregoing analysis, the rule advanced is unquestionably established. The leading case of *Morrison* v. *Work*, 266 U.S. 481 (1925), parallels this suit in that it was also an attempt by an individual tribal member to attack the management and disposition of tribal property and funds administered by the Secretary of the Interior, 266 U.S. at 483, and to claim that they were the individual property of the tribal members. The court said (266 U.S. at 485-486):

> * * *. It is admitted that, as regards tribal property subject to the control of the United States as guardian of Indians, Congress may make such changes in the management and disposition as it deems necessary to promote their welfare. The United States is now exercising, under the claim that the property is tribal, the powers of a guardian and of a trustee in possession. Morrison's contention is that, by virtue of the Act of 1889 and the agreements made thereunder, the ceded lands ceased to be tribal property and the rights of the Indians in the lands and in the fund to be formed became fixed as in-

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[3] It should be remembered that in suits touching the proper execution of a trust, the trustee is an indispensable party. *Thayer* v. *Life Association of America*, 112 U.S. 717, 719 (1885); *Osage Tribe of Indians* v. *Ickes*, 45 F.Supp. 179, 182, fn. 17 (D.D.C. 1942) aff'd, 133 F.2d 47 (C.A. D.C. 1943), cert. den., 319 U.S. 750. The United States occupies a position comparable to a trustee in supervising the tribal funds.

> dividual property. The Court of Appeals held this contention to be unfounded. We have no occasion to determine whether it erred in so ruling. The claim of the United States is, at least, a substantial one. To interfere with its management and disposition of the lands *or the funds* by enjoining its officials, would interfere with the performance of governmental functions and vitally affect interests of the United States. *It is, therefore, an indispensable party to this suit.* [Citing cases.] It was not joined as defendant. Nor could it have been, as Congress has not consented that it be sued. [Citing cases.] (Emphasis added.)

In that case, the plaintiff was attempting to enjoin the Secretary directly, while here appellant is attempting to do so indirectly, by enjoining the tribal officials, but the resultant interference with the performance of governmental functions is the same; indeed, this is an easier case than *Morrison*, because the same result is desired here and no attempt has been made to join even the Secretary.

In *Minnesota* v. *United States*, 305 U.S. 382 (1939), the State had attempted to condemn Indian lands and had joined the United States. The United States' motion to dismiss for lack of consent to suit had been denied in the trial court on the ground that the United States was not a necessary party and that consent had been granted by a named statute. The Supreme Court affirmed an appellate court reversal of the trial court, and stated (305 U.S. at 386-387):

> *First.* The United States is an indispensable party defendant to the condemnation proceedings. A proceeding against property in which the United States has an interest is a suit against

> the United States. (Citing cases.) It is confessedly the owner of the fee of the Indian alloted lands and holds the same in trust for the allottees. As the United States owns the fee of these parcels, the right of way cannot be condemned without making it a party. (Footnote omitted.) The exemption of the United States from being sued without its consent extends to a suit by a State. (Citing cases.)

The court made it clear in footnote 1, p. 386, that the key to the indispensability was not the nature of legal title held by the United States, but the historic relationship between the United States and the Indians. *Grand River Dam Authority* v. *Parker*, 40 F. Supp. 82, 85 (N.D. Okla. 1941); *Osage Tribe of Indians* v. *Ickes*, *supra*, p. 6, at p. 182, fn. 17. Similarly, in *United States* v. *Hellard*, 322 U.S. 363 (1944), the Court held that a partition proceeding that divested Indians of the Five Civilized Tribes of title to restricted land was invalid where the United States was not a party. The Court left no doubt that, absent congressional direction to the contrary, the United States must be present in suits dealing with Indian property. 322 U.S. at 367-368. Accord: *United States* v. *Candelaria*, 271 U.S. 432, 441-445 (1926); *Naganab* v. *Hitchcock*, 202 U.S. 473, 475-476 (1906); *Grand River Dam Authority* v. *Parker*, 40 F. Supp. 82, 84-86 (N.D. Okla. 1941); *First Nat. Bank of Holdenville, Okl.* v. *Ickes*, 60 F.Supp. 366, aff'd, 154 F.2d 851 (C.A.D.C. 1946) 370-371 (D. D.C. 1945); see *Barnes* v. *United States*, 205 F.Supp. 97, 100-101 (D. Mont. 1962). Although the fund here in question is not a restricted or trust

allotment of Indian land or direct proceeds from their sale, as was the subject matter in certain of the cited cases, the authority exercised by the United States in those cases is virtually identical with the control exercised here over the tribal judgment funds. Compare 25 U.S.C. sec. 409a, with Act of April 24, 1961, Pub. L. 87-24, 75 Stat. 45. The tribal funds are restricted in the same sense and the aim of the suit to divest the United States and the tribal entity of the fund is the same as in the cited cases, so that the identical considerations make the United States indispensable. As the court stated in *First Nat. Bank of Holdenville, Okla.* v. *Ickes, supra,* p. 8, at pp. 370-371:

> Since the object of the present suit is to declare invalid the Government's exercise of power under [certain statutes], the United States of America would be an indispensable party to the granting of the relief sought. It is firmly established that the United States has an interest in restricted Indian property, and that this interest of the sovereign may not be foreclosed by a judgment in proceedings in which the United States is not a party. (Citing cases.)

The name given to the interest of the United States or to the position it occupies has varied from case to case, but in each case one fact stands out with pristine clarity: When an attempt is made to divest the tribe of property over which the United States has retained supervisory control, the United States is an indispensible party to the proceeding. *Osage Tribe of Indians* v. *Ickes, supra,* p. 6, at p. 182, summarizes the United States' position:

> If the present case were to go to trial and judgment, and if in such a judgment plaintiffs' contention should maintained, it is obvious that the claim of the United States, that it is a trustee in possession, with power to act, would be decided against it without an opportunity to be heard.

The foregoing analysis illustrates that the United States has a substantial interest in a suit of this nature, that its presence is required, and that it cannot be joined because it has not consented to be sued. For those reasons, the district court correctly dismissed this suit.

III

THE DISTRICT COURT DOES NOT HAVE JURISDICTION OF THE SUBJECT MATTER

This suit is nothing more than an attempt to bring into the federal courts a tribal political question. As the Tenth Circuit said in a case very similar to this one, *Prairie Band of the Pottawatomie Tribe* v. *Puckkee*, 321 F. 2d 767, 770 (1963):

> In essence, this is a private civil dispute between Indians of the same Tribe and Band, concerning the method and procedure for distribution of the proceeds of a judgment, which have become tribal funds, to be distributed under the authority of the tribal governing body. It is an intra-tribal controversy, over which Federal court jurisdiction has been traditionally denied. See: *Martinez* v. *Southern Ute Tribe*, 249 F. 2d 915; *Native American Church* v. *Navajo Tribal*

Council, 272 F.2d 131; and *Dicke* v. *Cheyenne-Arapaho Tribes*, 304 F.2d 113.

Numerous other recent decisions make it clear that the federal courts do not have jurisdiction of the subject matter of suits involving internal tribal affairs, even when constitutional questions are sought to be raised. *Williams* v. *Lee*, 358 U.S. 217, 219-220 (1959); *Native American Church* v. *Navajo Tribal Council*, 272 F.2d 131, 133-135 (C.A. 10, 1959); *Barta* v. *Oglala Sioux Tribe of Pine Ridge Reservation*, 259 F.2d 553, 556-557 (C.A. 8, 1958), cert. den., 358 U.S. 932; *Iron Crow* v. *Oglala Sioux Tribe of Pine Ridge Res.*, 231 F.2d 89 (C.A. 8, 1956). Therefore, the district court correctly dismissed the suit.

IV

APPELLANT HAS NOT STATED A CAUSE OF ACTION

Even if procedurally, this suit would lie, it is plain that no cause of action has been stated. Cutting through the conclusory allegations of invalidity and illegality, we see that the real purpose of the suit is to compel a total per capita distribution of the seven million dollar judgment fund (R. 1, par. II; R. 2, par. V). The judgment fund is the result of a judgment obtained, under the Indian Claims Commission Act, against the United States and can be disbursed only pursuant to the congressional authorization. See 25 U.S.C. secs. 70t, 70u; *Minnesota Chippewa Tribe* v. *United States*, 315 F.2d 906, 914, fn. 11 (C. Cls. 1963). Congress has made that disbursement sub-

ject to several conditions, one of which is that all expenditures must be "authorized by the respective tribal governing bodies and approved by the Secretary of the Interior." 75 Stat. 45. The restriction is in accord with the paramount authority of Congress over tribal property. *Lone Wolf* v. *Hitchcock*, 187 U.S. 553, 568 (1903); *Tiger* v. *Western Investment Co.*, 221 U.S. 286, 311 (1911).

Appellant is in the contradictory position of wanting the benefits of the appropriation act but being unwilling to accept the conditions attached by Congress to the use of the funds appropriated. It is too well-established to require extended discussion that appellant has no individual vested interest in the fund. *Minnesota Chippewa Tribe* v. *United States*, 315 F.2d 906, 913-914 (C.Cls. 1963); see *Morrison* v. *Work*, 266 U.S. 481, 485 (1925). It is likewise clear that a party who benefits by a statute may not accept those benefits but claim that the conditions, restrictions, or limitations specified in the statute are invalid. As recently stated in *United States* v. *Kassan*, 208 F.Supp. 858 (S.D. Cal. 1962) at p. 861:

> * * * [T]he defendant, having requested and accepted the benefit of the Act and regulations, is estopped to claim this invalidity.

See *Federal Power Commission* v. *Colorado Interstate Gas Co.*, 348 U.S. 492, 501-502 (1955); 31 C.J.S., Estoppel sec. 110(8), pp. 580-581. In order to accept the benefits of this judgment fund, appellant must accept all of the conditions placed upon the use of that fund; he must accept those benefits and con-

ditions in common with the rest of the tribe and not under some claim of individual ownership of some portion of the fund. Congress has specified the procedure for expanding the fund, the Secretary and the tribal governing body have acted in exact accordance with that procedure and appellant has shown nothing that would justify judicial intervention in the procedure.

Thus, appellant has failed to state a cause of action and the district court correctly dismissed this suit.

CONCLUSION

For the foregoing reasons, the United States submits that the district court correctly decided this case and its judgment should be affirmed.

Respectfully,

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Assistant Attorney General.

SYLVAN A. JEPPESEN,
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APRIL 1964.

Certificate of Examination of Rules

I certify that I have examined the provisions of Rules 18 and 19 of the Ninth Circuit and that in my opinion the tendered brief is in compliance with all requirements.

Richard N. Countiss
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☆ U. S. GOVERNMENT PRINTING OFFICE: 1964 727921 863

No. 18,835

IN THE

United States Court of Appeals

For the Ninth Circuit

MARIA TERESA CRUZ SEGUI, as next friend on behalf of DIGNA LUZ ORTIZ, an infant and HECTOR LUIS ORTIZ, an infant,

Appellants,

vs.

RUTH SNOW BURNS O'ROURKE and JOHN P. O'ROURKE,

Appellees.

APPELLANTS' OPENING BRIEF

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PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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I

JURISDICTIONAL STATEMENT

This is an appeal from a final judgment of the United States District Court for the Southern District of California (Tr. 57-58), dismissing the complaint (Tr. 2-6) filed by Appellants, Plaintiffs below, against Appellees, Defendants below, for failure to state a claim upon which relief may be granted. The jurisdiction of the District Court was based upon diversity of citizenship under 28 U.S.C.A. § 1332. The jurisdiction of this Court is based on 28 U.S.C.A. § 1291.

II

STATEMENT OF THE CASE

On December 3, 1959, the United States District Court for the District of Puerto Rico entered a judgment (Tr. 8-13) in favor of Appellants herein, Plaintiffs below, against the corporation Snow Lines, Inc., for damages in the sum of $20,000.00 plus costs for the wrongful death of the Appellants' father as caused by the negligence of Snow Lines, Inc.[1]

The corporation Snow Lines, Inc. was duly organized and existed under and by virtue of the laws of

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[1]In its findings of fact and conclusions of law the Court found that Snow Lines, Inc. was the owner of a certain vessel known as the M/V Leda I, and that the corporation chartered, operated, managed, controlled, provisioned, manned, supplied and was in possession and control of said vessel. On March 17, 1954, Genaro Ortiz Esperanza, Appellants' deceased father, was employed by Snow Lines, Inc. aboard the vessel, and while he was attempting to carry out orders of the Master of the vessel to release a mooring line, the vessel, by reason of the negligence of corporation Snow Lines, Inc., its agents, servants or employees, was caused to collide with the dock, pinning the decedent between the vessel and the dock, thereby causing the decedent to sustain serious and severe injuries which resulted in his death. The Court further found that the injuries sustained by the decedent and his resulting demise were directly caused by the failure of the corporation Snow Lines, Inc., its agents, servants or employees, to provide a seaworthy, safe vessel and appliances and crew, and to keep the same in a seaworthy condition, and that the corporation failed, neglected and refused to supply the decedent with immediate and proper medical care, treatment, medication and nursing services which were reasonably necessary under the circumstances as a result of which his injury was caused to become more severe, aggravated and prolonged and to result in his death. The Court determined that Appellants herein, the recognized minor children of the decedent in whose behalf the action against Snow Lines, Inc. was brought, suffered damages in the amount of $20,000.00 as a result of the death of their father, and their consequent loss of his support, maintenance, love, care and affection, their expectation of inheritance, and their great mental anguish (Tr. 9-12).

the Commonwealth of Puerto Rico (Tr. 2, 9-10). It was originally incorporated on June 2, 1952, and its principal office was established in San Juan, Puerto Rico. The incorporators were Ruth Snow Burns, nineteen shares, John P. O'Rourke, nineteen shares, Vicente M. Ydrach, one share, and Walter L. Cox, one share. Vicente M. Ydrach, the attorney who organized the corporation, Snow Lines, Inc., and Walter L. Cox, one of the above-named original incorporators of Snow Lines, Inc., had resigned from and severed all connection with said corporation prior to the time Appellants' cause of action against the corporation for the death of their father arose, and prior to the time judgment was entered in their favor against the corporation on December 3, 1959 (Tr. 55).

Ruth Snow Burns O'Rourke and John P. O'Rourke were therefore the sole Directors and Shareholders of the corporation at all times relevant to the prior action against the corporation in the United States District Court of Puerto Rico and to the controversy which is the subject of this Appeal.

The sole asset of the corporation Snow Lines, Inc., was the vessel M/V LEDA I. On or about April 1, 1954, fourteen days after Appellants' deceased father sustained his injuries while working aboard said vessel, which injuries resulted in his death due to the negligence of Snow Lines, Inc., and therefore fourteen days after Appellants' rights as creditors arose against the corporation, the ship M/V LEDA I was conveyed by the Defendants John P. and Ruth Snow Burns O'Rourke, directors of Snow Lines, Inc., to one

Jose Oller, Jr. for the sum of $17,000.00, which amount was distributed by and between John P. and Ruth Snow Burns O'Rourke, making such distribution as Directors and receiving as Shareholders the total assets of the corporation thereby distributed (Tr. 46-47).

John P. and Ruth Snow Burns O'Rourke thereafter, and prior to the time the action was filed by Appellants in the District Court of Puerto Rico to seek damages for the wrongful death of their father, left the Commonwealth of Puerto Rico, and were not therefore available to be served with process and brought under the jurisdiction of that Court. The corporation, Snow Lines, Inc., has never, since that time, had any assets, engaged in business or maintained any place of business, or had any designated agent in the Commonwealth of Puerto Rico, and has not kept books or filed annual reports with the Secretary of the Treasury or the Secretary of State, as required under the laws of Puerto Rico. 3A Laws of Puerto Rico, Title 14, Private Corporations, Chapter 113, Section 2301.

The corporation Snow Lines, Inc., has never been formally dissolved by statutory proceedings as prescribed under the corporation law of Puerto Rico,[2] nor has its legal existence expired by any limitation of its term of existence or by forfeiture. While its corporate existence has not been terminated as a matter of law, however, the informal liquidation accom-

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[2]3A Laws of Puerto Rico, Title 14, Private Corporations, Chapter 110, Sections 2003, 2010, 2012.

plished by John P. and Ruth Snow Burns O'Rourke in the sale of its sole and therefore its total assets, the abandonment of its corporate activities, and the distribution of its property between themselves as shareholders, has resulted in its practical or *de facto* dissolution.

In their informal disposal of the corporate property, distribution of the proceeds and consequent termination of the corporate business, the Appellees, as the corporation's sole Directors and Shareholders, failed to take the proceedings prescribed by law for the protection of the corporation's creditors. Because of the informal liquidation of the corporation Snow Lines, Inc., accomplished by John P. and Ruth Snow Burns O'Rourke, and the unauthorized return of the corporation's entire capital to themselves as shareholders, Appellants have not been able to satisfy the judgment of December 3, 1959, against the corporation Snow Lines, Inc.

On December 3, 1962, Appellants, Plaintiffs below, filed a Complaint in the District Court of the United States for the Southern District of California against Snow Lines, Inc., Ruth Snow Burns O'Rourke, John P. O'Rourke, Vicente M. Ydrach, and Walter L. Cox, Defendants, seeking to recover the amount of the judgment debt in the amount of $20,000.00 from John P. and Ruth Snow Burns O'Rourke and other relief (Tr. 2-6). A certified copy of the Findings of Fact, Conclusions of Law and Judgment of the United States District Court for the District of Puerto Rico, filed and entered on December 3, 1959, in the prior

action against Snow Lines, Inc., was filed with the Complaint (Tr. 8-15).

On February 21, 1963, Appellees, Defendants below, Ruth Snow Burns O'Rourke and John P. O'Rourke, filed Notice of Motions pursuant to Rule 12b(1) and (6) for an order dismissing the action on the ground that the Court lacked jurisdiction over the subject matter and that the Complaint failed to state a cause of action upon which relief could be granted against said Defendants (Tr. 17-21).

On March 25, 1963, Appellants, Plaintiffs below, moved the Court for an order dismissing Defendants Snow Lines, Inc., Vicente M. Ydrach and Walter L. Cox, respectively, as parties defendant, on the ground that said parties had no real interest in or control over the subject matter of the controversy (Tr. 54-55).

A hearing was held in the District Court for the Southern District of California on Appellees' motion to dismiss; both Plaintiffs and Defendants were represented by counsel (Tr. 36). On the basis of the oral argument on March 25, 1963, and various memoranda submitted by Plaintiffs and Defendants (Tr. 24-36, 37-39, 45-53), the matter was submitted to the Court (Tr. 36), and on May 15, 1963, the Court filed its decision granting the Motion of Defendants John P. O'Rourke and Ruth Snow Burns O'Rourke to dismiss the Complaint as to them without leave to amend. The Court also approved and signed the Motion of Plaintiffs to dismiss as to the Defendants Snow Lines, Inc., Vicente M. Ydrach and Walter L. Cox (Tr. 56). Judgment was entered accordingly on June 4, 1963,

dismissing the action on the merits and with prejudice as to Defendants John P. O'Rourke and Ruth Snow Burns O'Rourke for failure to state a claim on which relief can be granted, and dismissing the action voluntarily as to all other Defendants (Tr. 57-58).

Notice of Judgment was mailed by the Clerk of the United States District Court for the Southern District of California on June 4, 1963 (Tr. 60), and on July 3, 1963, Appellants filed with that Court a Notice of Appeal to the United States Court of Appeal for the Ninth Circuit from that part of the Final Judgment entered on June 4, 1963, which dismissed the action on the merits and with prejudice as to Appellees Ruth Snow Burns O'Rourke and John P. O'Rourke (Tr. 62).

III

SPECIFICATION OF ERROR

Appellant has specified the following point on appeal:

The District Court erred in dismissing the complaint for failure to state a claim on which relief can be granted.

IV

ARGUMENT

I. THE ACTION WAS INSTITUTED IN THE COURT BELOW WITHIN THE PERIOD OF THE APPLICABLE STATUTE OF LIMITATIONS.

The District Court granted the motion of Defendants John P. O'Rourke and Ruth Snow Burns O'Rourke to dismiss Appellants' complaint without leave to amend as to them for failure to state a claim upon which relief can be granted (Tr. 57-58). In their statement of Points and Authorities, upon which the motion to dismiss was based, Appellees alleged that "[t]he theory of the complaint based upon negligence and alter-ego fails to state a cause of action against these defendants [Ruth Snow Burns O'Rourke and John P. O'Rourke] as it is barred by the statute of limitations" (Tr. 20).

Appellants asserted in their complaint, however, no "theory of the complaint based upon negligence," as contended by Appellees in the motion to dismiss, which would bar this action, as further contended by Appellees, under Section 340 of the California Code of Civil Procedure, which provides that an action for the death of a person caused by the wrongful act or neglect of another must be brought within a one year period of limitation. Appellants' earlier action in the District Court of Puerto Rico sought and resulted in a judgment awarding damages for the wrongful death of their father under the provisions of the Act of Congress approved June 5, 1920, known as the Mer-

chant Marine Act, amendatory to the Act of Congress known as the Seaman's Act of 1915, and by virtue of Section 20 of the latter Act, 46 U.S.C.A. § 688, which provides for recovery for injury to or the death of seamen. That section incorporated a three year limitation period. *Engel v. Davenport,* 271 U.S. 33 (1926).

The action brought by Appellants in the District Court of Southern California did not seek to establish the Appellees' personal liability for the wrongful death of the Appellants' deceased father, but sought to hold Appellees personally liable as directors and shareholders for the amount of a debt of the corporation Snow Lines, Inc., which debt arose out of the judgment of the United States District Court of the District of Puerto Rico entered on December 3, 1959. Their personal liability is imposed by statute and is based also on the fraudulent conduct of Appellees. The action is therefore within the purview of California Code of Civil Procedure, Section 338, which provides a three-year period for commencing such actions. Section 337.5 prescribes a ten-year period for commencing an action upon a judgment or decree of any court of the United States.

And insofar as the action arose in Puerto Rico, and therefore might be barred under the California law if barred by reason of the limitation period under Puerto Rican law, California Code of Civil Procedure Section 361, the action was instituted in the District Court for the Southern District of California within the period of limitations provided under the law of Puerto Rico.

Section 2202 of Chapter 112, Title 14, Private Corporations, 3A Laws of Puerto Rico (1962), provides as follows:

> "(a) When the officers, directors or stockholders of any corporation, shall be liable to pay the debts of the corporation, or any part thereof, any action to enforce such liability shall be a class action for the benefit of all creditors to which the corporation if in existence shall be a party.
>
> "(b) No suit shall be brought against any officer, director or stockholder for any debt or liability of a corporation, of which he is an officer, director or stockholder, until judgment be obtained therefor against the corporation, nor after three years from the date of such judgment and any such officer, director or stockholder may set up any defense which the corporation might have asserted against such debt or liability. This subsection (b) shall not apply to suits brought against officers or directors of a corporation in dissolution or liquidation for maladministration of their duties under chapter 110 of this subtitle."

Insofar as the liability alleged in Appellants' complaint arises under the statutory laws of Puerto Rico, the period of limitations imposed by the above-quoted statute, attaching the obtaining of a judgment against the corporation as a condition to the personal liability of corporate officers, directors and shareholders, is likewise applicable, and this action has been instituted within the prescribed period.

The California statute of limitations applicable to actions brought to enforce liability arising under for-

eign statutes is similar to Section 2202 of the Puerto Rican Law of Private Corporations, providing that such actions must be brought within three years after the liability was created, and the statute begins to run in bar of an action to enforce the personal liability of stockholders only after judgment has been given against the corporation and there exist no corporate assets from which to satisfy it. California Code of Civil Procedure, Section 359; *Bank of North America v. Rindge,* 57 Fed. 279 (1898); *Spencer v. Anderson,* 193 Cal. 1, 222 Pac. 355, 357 (1924).

II. THE COMPLAINT SETS FORTH FACTS SUFFICIENT TO STATE A LEGAL CLAIM AGAINST APPELLEES.

A. The complaint is sufficient as tested by the requirements of the Federal Rules of Pleading.

In testing the sufficiency of a complaint upon a motion to dismiss for failure to state a claim under Rule 12(b)(6) of the Federal Rules of Civil Procedure, 28 U.S.C.A., the allegations of the complaint should be viewed in a light most favorable to the plaintiff, assuming all well-pleaded facts to be true and indulging in all inferences which reasonably may be drawn therefrom. *Rennie & Laughlin, Inc. v. Chrysler Corporation,* 9 Cir., 242 F.2d 208 (1957).

In a recent case the United States Supreme Court, which seldom has to deal with matters of mere procedure, has put its full approval on the well-established standard, repeated in countless cases:

> "In appraising the sufficiency of the complaint we follow, of course, the accepted rule that a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson,* 355 U.S. 41, 45-46 (1957).

Further discussing the principle that the purpose of pleading is to facilitate a proper decision on the merits by the trial Court after a hearing on the proof, the Court stated in *Conley* that

> ". . . [T]he Federal Rules of Civil Procedure do not require a claimant to set out in detail the facts upon which he bases his claim. To the contrary, all the Rules require is a short and plain statement of the claim that will give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests. . . . Such simplified 'notice pleading' is made possible by the liberal opportunity for discovery and the other pretrial procedures established by the Rules to disclose more precisely the basis of both claim and defense and to define more narrowly the disputed facts and issues." 355 U.S. at 47-48.

This Court has also recently taken an opportunity to "reaffirm" its views on the granting of a motion to dismiss, in its opinion in *Rennie & Laughlin, Inc. v. Chrysler Corporation, supra,* 242 F.2d at 213:

> ". . . As stated in Gruen Watch Co. v. Artists Alliance, 9 Cir., 191 F.2d 700, 705,
>
> 'On occasion motions to dismiss supply a useful technique for the prompt disposition of suits,

and the Federal Rules of Civil Procedure which permit judgment on the pleadings are useful indeed. But it must be borne in mind that in many a suit such a motion cannot take the place of submission of evidence and of findings of fact and conclusions of law.'

Nor is a motion to dismiss the only effective procedural implement for the expeditious handling of legal controversies. Pretrial conference; the discovery procedures; and motions for a more definite statement, judgment on the pleadings and summary judgment, all provide useful tools for the sifting of allegations and the determination of the legal sufficiency of an asserted claim. The salvaged minutes that may accrue from circumventing these procedures can turn to wasted hours if the appellate court feels constrained to reverse the dismissal of an action. That is one of the reasons why a motion to dismiss is viewed with disfavor in the federal courts. Another is the basic precept that the primary objective of the law is to obtain a determination of the merits of any claim; and that a case should be tried on the proofs rather than the pleadings. DeLoach v. Crowley's Inc., 5 Cir., 128 F.2d 378, 380."

B. The facts alleged in the complaint were sufficient to notify appellees of the essence of the claim against them.

The complaint before the Court below alleges (Tr. 2-13) essentially the following:

On December 3, 1959, in the United States District Court for the District of Puerto Rico plaintiffs below obtained a judgment in their favor against the corporation Snow Lines, Inc., for the sum of $20,000

plus costs by virtue of a complaint claiming damages for the death of the plaintiffs' father, caused by the negligence of Snow Lines, Inc. Defendants below, Ruth Snow Burns O'Rourke and John P. O'Rourke, were alleged to be the sole stockholders, officers and directors in that corporation as to which facts were alleged which show it to have been *de facto* dissolved subsequent to the time appellants' cause of action arose.

It was further alleged by Appellants in their complaint filed below that Appellees had sold the sole known asset of the corporation, a ship known as the M/V LEDA I, "thereby rendering said corporation hopelessly insolvent for the sole and deliberate purpose of defrauding appellants herein, who are judgment creditors of said corporation," and that they have done so "to the prejudice of its creditors and to the plaintiffs in particular," and that they have unlawfully distributed between themselves the proceeds from the sale of the property which constituted the entire amount of assets of the corporation, "thereby rendering said corporation insolvent in that it did not have and does not have sufficient assets to pay its liabilities or discharge its debts which were then due and payable" and which payment "was not otherwise provided for."

C. It does not appear to a certainty that the appellants would not be entitled to relief under any set of facts which could be proved in support of the claim pleaded.

The purpose of the complaint was to hold Appellees Ruth Snow Burns O'Rourke and John P. O'Rourke

personally liable, as the sole stockholders, officers, and directors of a *de facto* dissolved corporation which served at all times only as their "alter ego" and business conduit, and as sole holders of the unlawfully distributed assets of the insolvent corporation, for a judgment debt of the corporation in favor of Appellants. There are several theories upon which such personal liability may be based, and the allegations of the complaint were sufficient to found the basis for the Appellants' claim for relief against the Appellees.

The Appellants did not attempt in their complaint, as Appellees contended in their motion to dismiss, to assert for the first time the negligence of the Appellees and to seek a judgment of the court below awarding damages therefor. Such action was pursued against the corporation Snow Lines Inc., in the United States District Court for the District of Puerto Rico and resulted in the award of a judgment to the Appellants against said corporation in the amount of $20,000 plus costs.

The action was then merged in the judgment which judgment gave rise to a new cause of action which is that brought in the Court below against the individual Appellees as officers and directors and as stockholders of the corporation Snow Lines, Inc. The rights of the Appellants against the Appellees, as directors and shareholders, did not arise until they had first obtained a judgment against the corporation upon which execution could not be levied, but the right which thereupon arose was one solely against the individual Appellees in their aforesaid capacities as

directors and shareholders of the corporation. It is a right which exists by virtue of the judgment rendered against the corporation but independent of the rights of the corporation itself which were merged in the judgment.

The sole asset of the corporation Snow Lines, Inc., was the vessel M/V LEDA I. It was aboard that vessel that on or about March 17, 1954, the Appellants' deceased father sustained severe injuries which resulted in his death, which injuries and his consequent demise were directly caused by the negligence of Snow Lines, Inc. On or about March 17, 1954, therefore, Appellants' rights as creditors arose against the corporation, even though their claim was contingent upon a judicial award. The relation of creditor and debtor arises in tort cases the moment a cause of action accrues and a claim exists by reason of which the creditor is or may become entitled to the payment of money. *Hansen v. Cramer,* 39 Cal.2d 321, 245 P.2d 1059 (1952); *Adams v. Bell,* 5 Cal.2d 697, 56 P.2d 208 (1936); *Freeman v. La Monte,* 148 C.A. 2d 670, 307 P.2d 734 (1957); *Cioli v. Kenourgios,* 59 Cal.App.690, 211 Pac.838 (1922). A corporation cannot by divesting itself of all its property leave remediless the holder of a claim in tort. *Pierce v. United States,* 255 U.S. 398, 402-03 (1921).

The conveyance of the ship M/V LEDA I by Appellees was generally alleged in the Complaint filed in the Court below. In support of that allegation, Appellants can prove that on or about April 1, 1954, the ship M/V LEDA I was conveyed by defendants,

John P. and Ruth Snow Burns O'Rourke, directors of Snow Lines, Inc., to one Jose Oller, Jr., for the sum of $17,000.00, which amount was distributed by and between John P. and Ruth Snow Burns O'Rourke making such distribution as directors and shareholders and thereby receiving as shareholders the total assets of the corporation.

1. Appellants as creditors of the corporation Snow Lines, Inc. have a direct right of action under common law principles against Appellees Ruth Snow Burns O'Rourke and John P. O'Rourke for their unlawful actions in disposing of the entire corporate property and distribution of the proceeds between themselves as shareholders without provision for and to the prejudice of its creditors.

A private corporation, in the absence of statute, may, under some circumstances, dispose of all its property by authority of its Directors or by vote of the majority of its Shareholders and divide the proceeds among its Shareholders, but only if its creditors are provided for and are not prejudiced thereby. *Bancroft v. Taylor,* 91 Fed.2d 579; *Calman v. Guaranty Security Corporation,* 271 Mass. 533, 171 N.E. 830, 834.

The liability of directors for declaration of dividends or distribution of assets when the payment thereof reduces the capital stock at a time when the capital of the corporation is impaired or the corporation is thereby rendered insolvent, provided the directors act in bad faith or are guilty of gross negligence or inattention, is a principle existing at common law

and is subject to an equitable remedy. *Aiken v. Peabody,* 7 Cir., 168 F.2d 615, 617 (1947); 12 Fletcher, *Cyc. Corp.* (Perm. Ed.), Section 5431.

If a solvent, going corporation divests itself of its assets by distribution among its shareholders, creditors and all others holding claims may sue the directors and shareholders under the theory that assets in the amount of the outstanding claims are impressed with a trust in favor of the creditors and may thus be followed into the hands of the shareholders. *Pierce v. United States,* 255 U.S. 398 (1921); *Bankers Trust Company v. Hale and Kilbourn Corporation,* 84 F.2d 401, 403 (1936); *Saracco Tank and Welding Company, Ltd. v. Platz,* 65 C.A. 2d 918, 150 P.2d 918, 924 (1944); Ballantine on Corporations, Sections 301, 318, pp. 7, 9-10, 732-33 (Rev. Ed. 1946).

It is well-settled that the officers and stockholders of a corporation are liable to its creditors for any acts by which their rights are injuriously affected and for any loss arising out of their fraud. Through Appellees' bad faith conduct as directors of the corporation Snow Lines, Inc., they rendered the corporation insolvent and unable to satisfy its judgment debt. The total assets of the corporation, the moneys obtained from the sale of the M/V LEDA I, may be traced into the hands of Appellees for the satisfaction of that debt in favor of Appellants.

2. Although Appellees' liability exists irrespective of statute, personal liability of Appellees for the judgment debt of the corporation is imposed by the law of

Puerto Rico, and the Complaint sufficiently alleges facts which support Appellants' claims thereunder.

By December 3, 1959, when final judgment was rendered by the United States District Court for the District of Puerto Rico in favor of Appellants against the corporation Snow Lines, Inc., said corporation was but a hollow shell, engaged in no activity and devoid of any assets. By their disposal of the sole property of the corporation, Appellees, John P. and Ruth Snow Burns O'Rourke, as directors of Snow Lines, Inc., and the division of the proceeds of that sale between John P. and Ruth Snow Burns O'Rourke, as shareholders, which division of proceeds constituted an unauthorized return of capital to themselves as shareholders, Appellants' rights of recovery on their judgment against the corporation have been defeated. Had it not been for the transfer and distribution in which they engaged, plaintiffs could have satisfied their liquidated claim out of the corporate assets.

Under generally accepted conflict of laws rules such matters concerning, the internal affairs of a corporation as the rights and liabilities of shareholders and directors are generally governed by the law of the state of incorporation. Restatement, Conflict of Laws §§ 182 et seq., 192 et seq.; *Signal Oil Co. v. Ashland Oil Co.,* 49 Cal. 2d 764, 774, 322 P.2d 1 (1958); *Southern Sierras Power Co. v. Railroad Commission,* 205 Cal. 479, 271 Pac. 747 (1928); *Sarocco Tank Co. v. Platz,* 65 C.A. 2d 306, 150 P.2d 918 (1944); *Pratt v. Odell & Co.,* 49 C.A. 2d 550, 122 P.2d 684 (1942).

Appellants as creditors of the corporation Snow Lines, Inc. have a direct right of action against Appellees Ruth Snow Burns O'Rourke and John P. O'Rourke for their unlawful actions in reducing the capital of the corporation and distributing its assets and thereby rendering it insolvent and unable to pay the claim upon which it was obligated to Appellants.

Section 1804 of the Law of Private Corporations, Chapter 108, Title 14, 3A Laws of Puerto Rico (1962), provides the procedures whereby a corporation existing under the laws of Puerto Rico may reduce its capital, providing that

> ". . . No such reduction, however, shall be made in the capital of the corporation unless the assets of the corporation remaining after such reduction are sufficient to pay any debts, the payment of which shall not have been otherwise provided for and the certificate shall so state."

Section 1804(e) then provides:

> "When any corporation shall decrease the amount of its capital as provided in this section, the certificate shall be published for three weeks successively at least once in each week, in a newspaper of general circulation published in this Commonwealth; the first publication to be made within fifteen days after the filing of such certificate, and in default thereof the directors of the corporation shall be jointly and severally liable to any creditors of the corporation who shall suffer loss by reason of the non-compliance with the provisions of this section and the stockholders shall be similarly liable up to the amount of such sums as

> they may respectively receive of the amount so reduced. . . ."

The allegations of the complaint sufficiently asserted the joint and several personal liability of Appellees, imposed under Section 1804 of the Puerto Rico Law of Private Corporations, as directors of the corporation for the full amount of the loss suffered by the Appellants as judgment creditors of the corporation by reason of the failure of Appellees to comply with the provisions of Section 1804.

It was alleged in the complaint that Appellees Ruth Snow Burns O'Rourke and John P. O'Rourke, as directors and stockholders of the corporation, sold and conveyed the sole asset of the corporation and distributed the proceeds between themselves, and thereby rendered the corporation insolvent and without sufficient assets to pay the debt owed by the corporation to Appellants and that the payment of such debt was not otherwise provided for.

As stockholders of the corporation, defendants are also liable to plaintiffs under Section 1804, to the extent that they hold wrongfully distributed assets of the corporation, i.e., up to the amount of such sums as they have received by reason of the distribution between them of the amount realized from the sale of the corporation's sole asset.

Section 1521 of Title 14, Chapter 105, of the Laws of Puerto Rico provides for the imposition of liability on directors for an unlawful payment of dividends. This section reads in relevant part as follows:

> "§ 1521. In case of any willful or negligent violation of the provisions of section 1520 of this title, the directors under whose administration the same may happen shall be jointly and severally liable, at any time within six years after paying such unlawful dividend, to the corporation and to its creditors, in the event of its dissolution or insolvency, to the full amount of the dividend unlawfully paid, with interest on the same from the time such liability accrued. . . ."

Section 1520 provides as follows:

> "§ 1520. No corporation created under the provisions of this subtitle, nor the directors thereof, shall pay dividends upon any shares of the corporation except in accordance with the provisions of this subtitle. Dividends may be paid in cash, in property, or in shares of the capital stock, in the case of shares with par value at par, and in the case of shares without par value at such price as may be fixed by the board of directors."

Section 1517 provides that dividends may only be paid out of available surplus or profits (net assets in excess of capital).

Unauthorized dividends include dividends not lawfully declared and also any illegal distributions of capital to stockholders, and the prohibition against unlawful payment of dividends applies regardless of whether any requisite formal action of the directors is observed in declaring the dividends, as where the stockholders of a corporation agree upon a distribution among the stockholders. See *Gray v. Sutherland,* 124 C.A.2d 280, 268 P.2d 754, 758 (1954); *Oilwell*

Chemical & Materials Co. v. Petroleum Supply Co., 64 C.A.2d 367, 148 P.2d 720 (1944).

A situation similar to that in the instant case obtained in *Snyder v. Yoder,* N.D. Ohio, E.D., 176 F. Supp. 617 (1959), an action by a judgment creditor of a corporation against directors of the corporation for an unauthorized distribution of stock rendering the corporation unable to satisfy the judgment.

That action was dismissed because it was not brought within the period of the applicable statute of limitations under Ohio law, which then required that such an action against directors by a creditor must be brought within one year after final judgment was rendered against the corporation in favor of the creditor. As pointed out, *supra,* the applicable statute under Puerto Rican law is three years, the same as that under California law, CCP § 359. It was held in the *Snyder* case, however, that the actions of the defendants, as directors of a *de facto* dissolved corporation, in transferring and distributing assets which rendered the corporation unable to satisfy the plaintiffs' adjudicated claim were the basis for imposing personal liability upon the directors under an applicable Ohio statutory provision similar to section 1521 of the Private Corporation law of Puerto Rico set out above.

In brief, by distributing between themselves the total assets of the corporation Snow Lines, Inc., i.e., the proceeds from the sale of its sole asset, the ship M/V LEDA I, the defendants Ruth Snow Burns O'Rourke and John P. O'Rourke rendered the corpo-

ration insolvent in defraud of the plaintiffs as creditors of the corporation. By reason of their acts in making this unlawful distribution of the corporate assets, i.e., paying an unlawful dividend, and thereby reducing the capital to render the corporation insolvent, defendants committed statutory violations on the basis of which personal liability is imposed upon them under common law principles and under the statutes of Puerto Rico for the amount of the judgment debt upon which the corporation is obligated to the plaintiffs. Section 2202 of Chapter 112, Title 14 of the Laws of Puerto Rico, set out above, provides, however, that this personal liability as directors and shareholders could be asserted against Appellees only after a judgment has been obtained against the corporation.

This action is one directly against and based upon the personal liability of the Appellees, Ruth Snow Burns O'Rourke and John P. O'Rourke. The obtaining of a judgment against the corporation Snow Lines, Inc., was, under section 2202 of Title 14 of the Laws of Puerto Rico, a condition precedent to the maintaining of an action against the Appellees as directors and shareholders of the corporation, and a failure to allege such a judgment in the body of the complaint would be fatal to the assertion of a claim therein.

Such judgment had been obtained by the Appellants, and the statutory requirement thereby fulfilled for the bringing of this action, as alleged in the complaint filed below. Appellees are therein alleged to be separately and independently liable for the judgment debt upon which the corporation was obligated to the

Appellants. No relief is sought in this action against the corporation and it is in no way a real party in interest in the action.

D. Appellants' complaint alleged facts supporting the alternate theory that the corporate entity of Snow Lines, Inc., should be disregarded and appellees should be held personally liable on the judgment against the corporation.

The complaint filed in the court below alleged that the corporation Snow Lines, Inc., in fact never had and does not now have any separate or genuine corporate existence, but was "used by the defendants for the purpose of permitting defendants to transact a portion of their individual business under a corporate guise," and that the corporation had been used by appellees "for the sole purpose of defrauding the plaintiffs herein, who are creditors of said corporation."

The appellees Ruth Snow Burns O'Rourke and John P. O'Rourke owned practically all the stock (38 of 40 shares), were the controlling directors and were in fact the only persons interested in the corporation, which was used as their instrumentality solely for the purpose of operating the corporation's sole asset, the ship M/V LEDA I.

The general rule is that courts will disregard the corporate entity when it is shown that there is such a unity of interest and ownership that the separateness of the dominating or controlling individuals and the corporation has ceased, and when failure to disregard the entity would sanction a fraud or promote injustice, that is, when the facts demonstrate misuse

of the corporate privilege or the need of limiting it in order to do justice. See *Ruberoid Co. v. North Texas Concrete Co.,* 5 Cir., 193 F.2d 121, 122 (1951); *Minifie v. Rowley,* 187 Cal. 481, 487, 202 Pac. 673, 676 (1921).

The issue is not whether the corporate entity should be disregarded for all purposes, nor need it be shown that the purpose of organizing the corporation was itself fraudulent or to defraud the plaintiff, but rather the issue is:

> "whether in the particular case presented and for the purpose of such case justice and equity can best be accomplished and fraud and unfairness defeated by a disregard of the distinct entity of the corporate form." *Kohn v. Kohn,* 95 Cal. App. 2d 708, 718, 214 P.2d 71 (1950).

Appellants maintain that in the instant case, Snow Lines, Inc., is the mere alter ego of defendants John P. and Ruth Snow Burns O'Rourke, and that the corporate entity should be disregarded and the judgment against Snow Lines, Inc., should be enforced as a judgment against the defendants individually, and that it is sufficient to justify such disregard of the entity if its recognition would produce an inequitable result. *Riddle v. Leuschner,* 51 Cal.2d 574, 581, 335 P.2d 107, 112 (1959).

In a case involving identical issues to those herein on very similar facts, the Supreme Court of Puerto Rico held that a complaint seeking to enforce a judgment debt of a corporation against individual shareholders was not subject to dismissal. The Court stated:

"We are aware that a corporation has a legal personality independent of its stockholders. But if the corporation is the mere 'alter ego' or business conduit of its only stockholders, with the benefits produced by the corporate business accruing exclusively and personally to them, then the stockholders shall be personally liable if it is necessary to prevent fraud or the accomplishment of an illicit purpose, or to prevent an injustice or a wrong. 1 Fletcher, op. cit., § 41, pp. 136, 139, and cases therein cited; Ballantine on Corporations, § 123, p. 294; Minifie v. Rowley, 202 Pac. 673; Gross v. Cohen et al., 58 So. 2d 703; Laughran v. Reynolds, 127 P.2d 586; Davis v. Perry, 120 Cal. App. 670, 8 P.2d 514; Pickwick Corp. v. Welch, 21 F. Supp. 664, 669; Hollywood Cleaning and Pressing Co. v. Hollywood Laundry Service, Inc., 217 Cal. 124.

"Within the rule of liberal interpretation of complaints as pleadings, the situation pointed out above arises substantially from the allegations of the complaint before us. Naturally, if the corporate entity is to be disregarded in a particular case, such action would depend upon the circumstances in each case, in the light of the general rules set forth above, and should be decided by the trial court after weighing the evidence. Stark v. Coker, 129 P.2d 399. We are not anticipating the merits of this case, nor holding that this is an adequate case, in accordance with the reality of the facts, to warrant application of the 'alter ego' or 'avoidance-of-fraud' rule set forth above. We confine ourselves to deciding that the complaint, considered separately, states sufficient facts to serve as a basis for the decision

of the case on its specific merits." *Cruz v. Ramirez,* 75 P.R.R. 889, 895-96 (1954).

CONCLUSION

It is submitted that the complaint filed by Appellants in the district court below contains sufficient allegations to invoke the jurisdiction of that court and to state a claim upon which relief may be granted, that appellees' motions to dismiss the complaint pursuant to Rule 12(b)(1) and (6) should have been denied by that Court, and that the judgment of that Court dismissing the complaint should be reversed.

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Edward R. FitzSimmons,
Ruth S. Harwitz,
Attorneys for Appellants.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Ruth S. Harwitz,
Attorney for Appellants.

No. 18,835

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

MARIA TERESA CRUZ SEGUI, as next friend on behalf of DIGNA LUZ ORTIZ, an infant and HECTOR LUIS ORTIZ, an infant,

Appellants,

vs.

RUTH SNOW BURNS O'ROURKE and JOHN P. O'ROURKE,

Appellees.

APPELLEES' BRIEF.

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vs.

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Appellees.

APPELLEES' BRIEF.

I.

JURISDICTIONAL STATEMENT.

The jurisdictional situation in this case is very complex and must be carefully scrutinized, especially since with respect to at least one, and perhaps two, of the primary theories of recovery advanced on appeal, there would be no jurisdiction in the District Court. In addition to being complex, the situation was, and is, made confusing by the fact that the Plaintiffs-Appellants, contrary to the express requirements of FRCP 8 (a)(1), failed to make any statement in the complaint of the basis of the District Court's jurisdiction.

Defendants-Appellees, among other motions, moved in the District Court for dismissal of the complaint for lack of jurisdiction because:

(a) Jurisdiction could not be based on diversity of citizenship (28 USCA §1332)[1] since there was not the required *complete* diversity in that plaintiffs and three of the defendants were all citizens of Puerto Rico [Tr. 18-19]. *Strawbridge v. Curtiss,* 3 Cranch 267, 2 L. Ed. 435 (U. S. 1806); Hart and Wechsler, *The Federal Courts and the Federal System,* 901 (1953); (Puerto Rico is deemed to be a *state* for purposes of determining diversity jurisdiction, 28 USCA §1332 (d)) and

(b) Jurisdiction could not be based on there being a claim arising under federal law (28 USCA §1331)[2] as a claim based on a prior federal court judgment is a state created cause of action and does not provide a basis of federal jurisdiction [Tr. 20]. *Provident Safe Life Insurance Society v. Ford,* 114 U. S. 635; *Metcalf v. Watertown,* 128 U. S. 586 (1888).

Plaintiffs-Appellants recognized below that the only possible basis of jurisdiction was diversity of citizenship and, therefore, voluntarily moved for dismissal of

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[1]Section 1332. Diversity of citizenship; amount in controversy, (a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $10,000 exclusive of interest and costs, and is between: (1) Citizens of different States; . . .

[2]Section 1331. Federal question; amount in controversy. The district courts shall have original jurisdiction of all civil actions wherein the matter in controversy exceeds the sum or value of $10,000 exclusive of interest and costs, and arises under the Constitution, laws or treaties of the United States.

the three non-diverse Defendants including the corporate Defendant Snow Lines, Inc. [Tr. 54] and said motion was granted [Tr. 56]. The District Court then had jurisdiction with respect to those theories of recovery urged by Plaintiffs as to which the voluntarily dismissed Defendants were not indispensable parties, and the complaint was then dismissed, not for lack of jurisdiction, but because the complaint failed to state a cause of action [Tr. 58].

In the opening brief on appeal, Plaintiffs-Appellants state that jurisdiction in the District Court was based solely on diversity of citizenship (App. Br. p. 1). If Appellants in the opening brief had restricted themselves to arguing the substantive theories of relief most strongly urged in the District Court, and as to which the voluntarily dismissed Defendants were not indispensable parties, Appellees would agree that the District Court had jurisdiction once the three Puerto Rico Defendants were dismissed, and that said jurisdiction was based on diversity of citizenship. However, in the opening brief, a theory, based upon §2202 of Chap. 112, Title 14, Private Corporations, 3A Laws of Puerto Rico (1962), is being advanced by Appellants (App. Br. p. 10) with respect to which there would be *no* jurisdiction in the District Court based on diversity of citizenship (or otherwise) for the reason that Snow Lines, Inc., one of the voluntarily dismissed and non-diverse Defendants, is an indispensable party to any claim based on said statutory theory. It is hornbook

law that where an indispensable Defendant has the same citizenship as the Plaintiffs there is no diversity of citizenship sufficient for federal jurisdiction.

> "[I]f a non-diverse party to a controversy is indispensable, *Strawbridge v. Curtiss* obviously defeats federal jurisdiction altogether. Action cannot be brought without him; and, if he is joined, an amendment to dismiss him is unavailing." *Hart and Wechsler, supra,* p. 908; *Dollar SS Lines v. Merz,* 68 F. 2d 594 (9th Cir. 1934).

That the non-diverse and voluntarily dismissed corporate defendant, Snow Lines, Inc., is an indispensable party to any claim founded on §2202 is clear from reading that section itself[3] wherein it is stated that "that the corporation, if in existence, *shall* be a party" (emphasis added). This language is mandatory and not permissive. There can be no doubt that the corporation is in existence and thus an indispensable party, regardless of appellants' frequent characterizations of it being something called "de facto dissolved".

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[3]Section 2202 of Chapter 112, Title 14, Private Corporations, 3A Laws of Puerto Rico (1962), provides as follows:

"(a) When the officers, directors or stockholders of any corporation, shall be liable to pay the debts of the corporation, or any part thereof, any action to enforce such liability shall be a class action for the benefit of all creditors *to which the corporation if in existence shall be a party.* (Emphasis added.)

"(b) No suit shall be brought against any officer, director or stockholder for any debt or liability of a corporation, of which he is an officer, director or stockholder, until judgment be obtained therefor against the corporation, nor after three years from the date of such judgment and any such officer, director or stockholder may set up any defense which the corporation might have asserted against such debt or liability. This subsection (b) shall not apply to suits brought against officers or directors of a corporation in dissolution or liquidation for maladministration of their duties under chapter 110 of this subtitle."

As a matter of fact and of record, the corporation is presently, and at all times of relevance to this action has been, fully in existence. In the judgment obtained in the District Court of Puerto Rico by these plaintiffs, which judgment is attached to and incorporated in the complaint, it is expressly so held. Finding of Fact No. 1 [Tr. 9] states that "the defendant, Snow Lines, Inc., was and now is a corporation, duly organized and *existing* under and by virtue of the laws of the Commonwealth of Puerto Rico" (emphasis added). Findings 2 and 3 [Tr. 10] recite that Snow Lines, Inc. was the owner of the vessel involved and that Snow Lines, Inc. charted, operated, managed, controlled, provisioned, manned, supplied and was in possession and control of the said vessel. Said judgment, which was obtained by *these Plaintiffs* in an action in which only they appeared, recites the existence of the corporation on December 3, 1959, the date on which the judgment was entered. Yet appellants seek to assert in their brief that the corporation was "de facto dissolved" in 1954, five years earlier. At page 3 of their brief, appellants assert that on April 1, 1954 the corporation disposed of its sole asset, the MV LEDA I. At page 4, appellants assert that *prior* to the time of the filing of the action in Puerto Rico, the corporation had disposed of all of its assets, had not engaged in any business or had any place of business, nor filed proper annual reports, and, therefore, was de facto dissolved. But, despite these statements and allegations, the District Court in Puerto Rico in Plaintiffs' own lawsuit found as a matter of fact that the corporation was in existence long *after* the alleged date of the alleged de facto dissolution.

Even in the absence of such a complete collateral estoppel against Appellants arguing lack of corporate existence, it is clear that for the purposes of Section 2202 the corporation is fully in existence. Appellants recognize at page 4 of their brief that the corporation "has never been formally dissolved by statutory proceedings as prescribed under the corporation law of Puerto Rico, nor has its legal existence expired by any limitation of its term of existence or by forfeiture". If Appellants' theory of *de facto* dissolution could be utilized to eliminate the requirement of Section 2202 that the corporation be joined as a party in this case where *the legal existence is recognized by all parties,* it would be a complete emasculation of that requirement. Section 2202 establishes a remedy, under special circumstances, against the individuals connected with a corporation where it is deemed that the normal corporate limitation of liability should not apply. In substantially all such circumstances, a case could be made out that the corporation was "non-existent" or "an alter ego" or "de facto dissolved" because those are the very situations in which such suits against officers, directors and stockholders become possible. If the theory of a so-called "de facto dissolution" would be sufficient to remove the necessity under Section 2202 for joining the corporation as a party, it would have to be found that the Puerto Rican legislature added the express requirement of joinder for no purpose. Surely, the Puerto Rican legislature was entitled to require that a corporation should at least be made a party to an action in which its very existence could be declared a fraud and which existence could be completely denied. The corporation is entitled to litigate this point. The over-

whelming presumption is that the legislature meant what it said in absolutely requiring that the corporation be joined as a party. In this regard, it should be noted that Puerto Rican Legislature has provided a means for terminating the existence of corporation which fails to comply with the Puerto Rican laws. Section 2302 of Chap. 112, Title 14, Private Corporations, 3A Laws of Puerto Rico (1962) provides for such termination through *Quo Warranto* proceedings where a corporation fails to file the necessary reports or keep required books. Plaintiffs-Appellants never availed themselves of such procedure and the corporation remains fully in existence.

Accordingly, to the extent that the complaint may be based on an asserted claim under Section 2202 of the Corporate Law of Puerto Rico, there is no jurisdiction in the District Court because an indispensable party Defendant, Snow Lines, Inc., is a citizen of the same state as are Plaintiffs. With respect to the Appellants' remaining theories, there is sufficient jurisdiction in the District Court under 28 USCA 1332 to find that the complaint fails to state a claim for relief. The jurisdiction of this Court is based on 28 USCA Section 1291.

II.

STATEMENT OF THE CASE.

Since the only facts that may be considered on this appeal are those set forth in the complaint, Appellees will, for the purposes of this appeal, not set forth their own statement of the case, but will make their argument based on Appellants' statement of the case.

III.
ARGUMENT.

1. Introduction.

Appellants are asserting several alternate theories in an attempt to support a claim upon which relief can be granted. These theories are alternately based on Section 2202 of the Puerto Rico Corporations Code, *supra* [see footnote 1]; on a theory of *alter ego;* on a theory of common law fraudulent conveyance; and on a theory based on Section 1804, Laws of Private Corporations, Chap. 108, Title 14, 3A Laws of Puerto Rico. None of these theories can prevail, as more fully discussed below.

2. Even Were Appellants Able to Make Out a Claim Under §2202, the District Court Would Have No Jurisdiction to Hear Such Claim; Moreover, an Indispensable Party to Any Claim Based on §2202 Has Been Dismissed From the Action.

(a) The District Court Has No Jurisdiction of Any Claim Based on §2202.

For the reasons discussed above, in the Jurisdictional Statement, this action cannot be based upon Section 2202 for the reason that the Corporation, Snow Lines, Inc., is an indispensable party Defendant and of the same citizenship as Plaintiffs and, accordingly, the District Court would have no jurisdiction.

(b) An Indispensable Party Under §2202 Has Been Voluntarily Dismissed and the Action Cannot Be Maintained in Its Absence.

Regardless of the lack of jurisdiction, the action could not be maintained under Section 2202 because the corporate Defendant, Snow Lines, Inc., was voluntarily

dismissed by Plaintiffs and, pursuant to the very terms of Section 2202, the Corporation is an indispensable party. (See the extensive discussion in the Jurisdictional Statement, *supra,* pp. 1 to 7) It is elementary that a court cannot hear an action in the absence of an indispensable party.

Of course, Appellants are in a dilemma in this regard. Because the corporation is an indispensable party, the action cannot proceed in its absence and, on the other hand, if the corporation is made a party there is no federal court jurisdiction. This is an aspect of the limited nature of the federal district court jurisdiction. The action could be brought in a state court without this dilemma, as a diversity of citizenship, of course, is not a requirement of state court jurisdiction. For a discussion of this dilemma in reference to other analogous cases, see *Hart and Wechsler, supra,* p. 908.

3. Alter Ego, Even if Established, Does Not Have the Effect Claimed by Appellants and Cannot Support the Cause of Action in This Instance; Moreover, Appellants Are Collaterally Estopped From Asserting That Doctrine.

(a) Alter Ego, Even if Established, Cannot Convert a Judgment Against One Person Into a Judgment Against Another Who Was Not a Party to That Action.

The theory of *alter ego* was the one primarily pressed in the trial court and as to which most of the papers filed below were addressed. Appellants' theory is basically this: they have a judgment against the corporation, Snow Lines, Inc.; Snow Lines, Inc. is a sham and only the *alter ego* of the individual Defendants and, accordingly, the individual Defendants should be

held liable. Assuming Appellants' facts to be correct, certain elements of this argument are plausible and give a certain apparent attractiveness to the whole theory. However, the theory contains a fatal defect. This is most clearly pointed out in the California case of *Minton v. Cavaney,* 56 Cal. 2d 576, 364 P. 2d 473 (1961). In that case, the plaintiff sued a director of a corporation on the grounds that the corporation was a sham and that he was the *alter ego.* Plaintiffs, as here, had previously obtained a judgment against the corporation. The court properly pointed out that if it was established in the lawsuit that the corporation was a sham, the defendant director would lose the limitation of liability that the corporation would normally impose and he would be left without the corporate shield. This would *permit* the director to be sued directly, but *he would have to be sued on the original cause of action,* the negligence cause of action. He cannot be sued upon the judgment as the judgment was not against him. One person cannot be sued upon the basis of a judgment against another person. This is elementary due process. United States Constitution, Article 5; Puerto Rico Constitution, Article 2, Section 7.[4] However, Appellants repeatedly make it clear that they are *not* suing on a theory of negligence but are attempting to sue upon the judgment itself (App. Br. p. 5). Appellants argue (App. Br. p. 5) that the negligence action was *merged* in a judgment which gave rise to a *new cause of*

[4]"No person shall be deprived of his liberty or property without due process of law."

action which was brought in the court below against Appellees.

Appellants are attempting to change a sow's ear into a silk purse. A judgment against one party simply cannot be converted into a judgment against someone else. Appellants fail to distinguish between the benefits of the *alter ego* doctrine which permits them to sue Defendants based upon the original cause of action and a completely erroneous notion of due process which would permit them to sue Defendants directly upon the judgment obtained against someone else, to wit: the corporation.

The case of *Minton v. Cavaney, supra,* is a California case. However, its theory is not peculiar to California law but is based solidly on principles of due process. There appears to be no comparable case in Puerto Rico but it should be noted that Puerto Rican courts do refer to California courts for analogous authority on the *alter ego* doctrine. See *Swiggert v. Swiggert,* 55 P. R. R. 72 in which the Puerto Rican court followed California law in establishing other elements of the *alter ego* situation.

(b) Plaintiffs-Appellants Are Collaterally Estopped From Asserting That the Corporation Is a Sham and the Alter Ego of the Individual Defendants.

In their suit against the Corporation, Snow Lines, Inc., in the District Court of Puerto Rico, Plaintiffs obtained a default judgment in an action in which only they appeared and the judgment in that action is attached to and incorporated in the present complaint.

Said judgment absolutely refutes any contention that the Corporation was a sham or an *alter ego* and completely collaterally estops Plaintiffs from maintaining such a claim. The first four findings of fact in said judgment obtained by Plaintiffs are as follows [Tr. 9-10]:

> 1. The defendant, Snow Lines, Inc. was and now is a corporation, duly organized and existing under and by virtue of the laws of the Commonwealth of Puerto Rico.
>
> 2. The defendant was the owner of a certain vessel known as the M/V LEDA I.
>
> 3. The defendant chartered, operated, managed, controlled, provisioned, manned, supplied and was in possession and control of the aforesaid vessel.
>
> 4. On the 17th day of March, 1954, Genaro Ortiz Esperanza, deceased, was in the employ of the defendant and the defendant employed the decedent aboard the aforesaid vessel.

It is clear from said findings that it has been judicially decided, at Plaintiffs' own behest, that the Corporation was in existence and actually owned, operated and controlled the vessel on which the injury was alleged to have occurred and that the Corporation was the employer of the seaman. Note, particularly, the findings that the Corporation was *duly* organized *and existing* at the time of the accident and five years following at the date of judgment.

4. Appellants' Claimed Common Law Cause of Action in the Nature of Fraudulent Conveyance Cannot Prevail as There Is No Such Common Law Doctrine in Puerto Rico and Even if There Were It Would Now Be Barred by the Statute of Limitations.

(a) There Is No Common Law Cause of Action in Puerto Rico—a Land Having Its Legal Orgins in the Spanish Civil Code.

Appellants assert that common law principles will provide a basis for liability in that the Defendants caused the Corporation to improperly distribute its assets to Defendants. It is interesting that Appellants cite no Puerto Rico cases in this regard, nor do they cite Puerto Rican statutes on fraudulent conveyances.

The reason for the failure to cite Puerto Rican statutes on fraudulent conveyances is that there is nothing in the Puerto Rican law resembling the statutory codification of fraudulent conveyances as found in California and in many other states.

As to common law principles, as aforesaid, no cases are cited. As a matter of fact (and foreign law is a matter of fact to be pleaded and proved by Plaintiffs) it is doubtful that the common law exists in Puerto Rico, especially with regard to fraudulent conveyances. For example, Section 5141 of Chap. 393, Laws of Puerto Rico, Annotated, is the statutory embodiment of the basis of tort claims based on fault or negligence. Fraud is one of the subtitles covered under this statutory rubric. (See the Annotations to the above section in the Laws of Puerto Rico, Annotated). The case of *Rivera v. Central Park Opasto Viejo Incorporated,* 44 P. R. R. 236 (1932) indicates that with respect to the

the interpretation of Section 5141, the courts of Puerto Rico are not bound by common law, or by interpretations given by courts of the United States to statutes in force in the United States. The Annotations indicate that the reason for this is because Section 5141 was derived from the *Spanish Civil Code,* Art. 1902 and not from the common law.

(b) Statute of Limitations Would Have Barred Any Such Cause of Action.

Even if there were such a common law doctrine of fraudulent conveyance in Puerto Rico, which it seems apparent there is not, any cause of action based thereon would be barred by the statute of limitations.

Section 5298 of Title 31 of the Laws of Puerto Rico[5] provides that actions arising under Section 5141 (actions based on fault including fraud) must be brought within one year. This action was brought approximately eight years following the alleged fraudulent transfer. Compare California Code of Civil Procedure, Section 338[6] which bars a cause of action for fraudulent conveyance after three years. Note also that California Code of Civil Procedure, Section 361,[7] will bar

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[5]"The following prescribe in one year . . .

"2. Actions to demand civil liability for obligations arising from the fault or negligence mentioned in §5141 of this Title, from the time the aggrieved party had knowledge thereof."

[6]"Within three years: . . .

"1. An action upon a liability created by statute, other than a penalty or forfeiture. . . .

"4. An action for relief on the ground of fraud or mistake. The cause of action in such case not to be deemed to have accrued until the discovery, by the aggrieved party, of the facts constituting the fraud or mistake."

[7]§361. Limitation laws of other states, effect of. When a cause of action has arisen in another state, or in a foreign country, and by the laws thereof an action thereon cannot there

a cause of action in California as soon as it would be barred under Puerto Rican law. Thus, any cause of action based upon some alleged common law principle of fraudulent conveyance would have been barred several years ago.

5. Even Were Appellants Able to State a Claim Under §1804, That Claim Would Either Be Barred by the Statute of Limitations or Would Be One With Respect to Which the District Court Has No Jurisdiction.

Appellants assert that facts as set forth in the complaint indicate that an unlawful dividend or reduction of capital was made by the Corporation in violation of Section 1804, Puerto Rican Corporations Code[8] (App. Br. p. 20). Appellants then argue that pursuant to the combined effect of Sections 1520 and 1521, Title 14, Chap. 105 of the Laws of Puerto Rico,[9] Defendants

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be maintained against a person by reason of the lapse of time, an action thereon shall not be maintained against him in this state, except in favor of one who has been a citizen of this state, and who has held the cause of action from the time it accrued.

[8]". . . No such reduction, however, shall be made in the capital of the corporation unless the assets of the corporation remaining after such reduction are sufficient to pay any debts, the payment of which shall not have been otherwise provided for and the certificate shall so state."

[9]§1520. No corporation created under the provisions of this subtitle, nor the directors thereof, shall pay dividends upon any shares of the corporation except in accordance with the provisions of this subtitle. Dividends may be paid in cash, in property, or in shares of the capital stock, in the case of shares with par value at par, and in the case of shares without par value at such price as may be fixed by the board of directors.

§1521. In case of any willful or negligent violation of the provisions of section 1520 of this title, the directors under whose administration the same may happen shall be jointly and severally liable, *at any time within six years after paying such unlawful dividend,* to the corporation and to its creditors, in the event

are made personally liable for such improper dividends (App. Br. pp. 21-22). However, Section 1521, which provides a remedy against individual directors for a corporation's unlawfully declaring a dividend or improperly reducing its capital, expressly provides that a cause of action must be brought within six years after the payment of such unlawful dividend, or such improper reduction in capital. In this case, the alleged distribution was made in 1954 [App. Br. pp. 3-4; Tr. 46-47]. Accordingly, any action based on Sections 1804 and 1521 were barred in 1960, two years before the institution of this action.

Appellants seek to avoid this bar by arguing that in fact the statute of limitations provided in Section 2202[10] applies. If, in fact Section 2202 did apply then the statute of limitations would not have run until three years after the judgment was obtained against the Corporation and thus this action would be timely according to Appellants' argument. However even were Appellants' argument accepted in spite of the fact that Section 1521 expressly carries its own statute of limitations, this would avail Appellants nothing as Section 2202 requires that the Corporation be made a party. As more fully argued under the Jurisdictional Statement (pp. 1 to 7) and under subparagraph 2 above regarding Section 2202 (pp. 8 to 9), where said Sec-

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of its dissolution or insolvency, to the full amount of the dividend unlawfully paid, with interest on the same from the time such liability accrued. . . . (Emphasis added.)

[10]See footnote 1.

tion 2202 applies there can be no jurisdiction in the District Court because an indispensable party Defendant is missing and because that indispensable party is of the same citizenship as the Plaintiffs and would destroy jurisdiction based upon diversity of citizenship.

Conclusion.

For the reasons set forth above, the judgment of the District Court should be affirmed.

SCHWAB & KANT,
By HAROLD S. KANT,
Attorneys for Appellees.

Certificate.

I certify that in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing brief is in full compliance with those rules.

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APPELLANTS' REPLY BRIEF

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APPELLANTS' REPLY BRIEF

Appellees first argue in their brief that appellants are "collaterally estopped" from asserting the non-existence of the corporation Snow Lines, Inc. (hereinafter referred to as the corporation), and therefore the complaint must fail because the corporation was not joined as a party defendant in the action filed below.

They further assert that appellants are estopped from claiming that the corporation is but defendants' alter ego for the purpose of holding defendants per-

sonally liable upon the judgment against the corporation. Appellees refer to appellants' attempt to "make out a claim under § 2202" of the Puerto Rico Corporations Code and to appellants' "claim based on § 2202" (Appellees' Brief, p. 8).

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1. **APPELLANTS DO NOT ASSERT ANY "CLAIM UNDER § 2202"; SECTION 2202 IS RATHER A STATUTE WHICH SETS FORTH THE CONDITIONS WHICH MUST BE MET IN BRINGING AN ACTION UNDER PUERTO RICAN LAW AGAINST DIRECTORS OR STOCKHOLDERS OF A CORPORATION WHEN THEY ARE LIABLE TO PAY THE DEBTS OF THE CORPORATION.**

The liability of the appellees to pay the judgment debt of the corporation is based not upon section 2202, which itself imposes no such liability, but upon sections 1521 and 1804 of the Puerto Rico Law of Private Corporations, set out in Appellants' Opening Brief at pages 20 and 22, and upon the common law.

Appellees have argued in their brief at length (pages 3-6, 8-9, 16-17) that the corporation is an indispensable party defendant under section 2202, the non-joinder of which in the action deprives the District Court of jurisdiction.

Appellants submit that appellees have improperly raised for the first time on this appeal the objection that the corporation is an indispensable party to the action. This point was not asserted in the Court below and was not before that Court for consideration in the rendering of its decision on appellees' motion

below. The argument is properly raised on further motion under Rule 19 of the Federal Rules of Civil Procedure, 28 U.S.C.A., in the trial Court and, if well taken by that Court, appellants should have the opportunity to amend their complaint to join the corporation.

Appellees asserted in the Court below (Tr. 18-19), and argue further in their brief on appeal (pages 2-4, 7, 17) only that the joinder of the corporation as a party defendant destroyed the jurisdiction of the District Court as based on diversity of citizenship, under 28 U.S.C.A. § 1332 (Appellees' Brief, p. 2). Appellees below in fact argued that the joinder of the corporation destroyed diversity *though they need not have been joined* (Tr. 19).

When it was made clear to appellants that the Court below intended to dismiss on the basis of non-diversity, and since they were not faced with the argument that the corporation was an indispensable party, appellants moved to dismiss the corporation as a party defendant (Tr. 54-55), though the appellants had argued their position below that their joinder as a nominal or formal party did not in any event destroy diversity jurisdiction in the District Court (Tr. 52-53).

Section 2202, Chapter 112, Title 14, Private Corporations, 3A Laws of Puerto Rico, has been set forth by Appellants in their Opening Brief at page 10 and appears as Footnote 3 in Appellees' Brief at page 4. Section 2202(a) provides that an action to enforce the liability of directors or stockholders of a corpo-

ration to pay the debts of the corporation "shall be a class action for the benefit of all creditors to which the corporation if in existence shall be a party."

Section 2202 does not require that the corporation shall be joined as a party *defendant*. It would be better argued, particularly in view of the fact that directors' liability under section 1521 of the Corporation law is imposed in favor of both the corporation and its creditors, that the corporation might be more properly joined as a party *plaintiff*, and thus, even if joined as a nominal party defendant because of the impossibility of obtaining its consent to such joinder as a plaintiff, such joinder as a nominal party defendant would not destroy diversity.

Furthermore, the appellants could not in any event be estopped by a finding that the corporation was in existence in December 1959 from asserting that the corporation no longer had any valid existence in December 1962. The complaint below, filed December 3, 1962, alleges that the corporation "has for at least three years next preceeding the filing of this complaint" had no known place of business or named agent and had failed to keep its books or file annual reports as required by the laws of Puerto Rico (Tr. 2, 3). It was further alleged in the complaint that on a date *subsequent* to the entering of the Judgment of December 3, 1959, the appellees conveyed the corporation's sole asset and distributed between themselves the proceeds from said conveyance, thereby rendering the corporation insolvent and unable to pay its judgment debt to appellants (Tr. 5).

Appellants subsequently learned and stated in their memorandum below (Tr. 46) and in their Opening Brief on Appeal at page 3, that the corporation disposed of its sole asset in April 1954. The appellants have not stated when the unlawful distribution of the proceeds from that sale was made as they do not have knowledge of when this act, which constituted the ultimate fraud alleged and incurred the statutory liability of appellees as directors and shareholders of the corporation, was performed by the appellees.

Even if appellants were estopped from denying the existence of the corporation prior to December 3, 1959, the Judgment rendered that date cannot be binding as to or even evidence of its continued existence subsequent to that date, nor in any way does the Judgment estop the appellants from asserting the de facto dissolution of the corporation and denying the existence of the corporation which renders unnecessary under section 2202 its joinder as a party in this action filed December 3, 1962.

The naming of the corporation as a party to the action is of course unnecessary to the maintenance of the action on the common law theory of appellees' personal liability for the corporation's judgment debt. No relief is sought in the action against the corporation and it is in no way a real party in interest in the action.

2. APPELLANTS' ACTION AS BASED UPON APPELLEES' STATUTORY LIABILITY UNDER PUERTO RICAN LAW WAS FILED IN THE COURT BELOW WITHIN THE APPROPRIATE PERIOD OF LIMITATIONS.

Chapter 41 of Title 32, Code of Civil Procedure, 8 Laws of Puerto Rico Annotated, sets forth the statutory provisions relating to the time of commencing civil actions. Section 261 of that chapter provides as follows:

> "§ 261. This part does not affect actions against directors or stockholders of a corporation, to recover a penalty or forfeiture imposed, or to enforce a liability created by law; but such action must be brought *within three years after the discovery by the aggrieved party of the facts upon which the penalty or forfeiture attached or the liability was created.*" (Emphasis added.)

We find no Puerto Rican cases under this section, but the statutory history states that the above-quoted provision was derived from section 359 of the California Code of Civil Procedure, the language of which is essentially identical to that of section 261 above and under which there have been numerous Court decisions.

It has been well established that the term "created by law," as used in this section is confined and restricted to liability existing by virtue of express statute and does not include or extend to actions arising under common law.

> *Southern Counties Thrift Co. v. Rairdon*, 47 Cal.App.2d 770, 118 P.2d 828 (1941);
>
> *Coombes v. Getz*, 217 Cal. 320, 18 P.2d 939 (1933).

This three-year statute clearly therefore does not bar the action as based upon the appellees' common law liability, as set forth in Appellants' Opening Brief at pages 17-18, and as established under the law of Puerto Rico as discussed below.

Nor does this statute bar appellants' action to enforce the statutory liability of appellees as directors or shareholders of the corporation imposed under sections 1521 and 1804(e) of the Puerto Rican Law of Private Corporations, Title 14, 3A Laws of Puerto Rico (1962).

The "facts upon which . . . the liability was created" under these sections were, it is true, the sale of the corporation's sole asset, which it is now known occurred in 1954, and the unlawful distribution of the corporate assets between the appellees, which occurred at some date still unknown to appellants. Neither of these sets of facts was *discovered* by appellants, however, until they had obtained a judgment against the corporation, execution upon which was returned unsatisfied due to the then-discovered insolvency of the corporation, caused by the subsequently discovered aforesaid acts of appellees.

This action was thereupon instituted by appellants in the District Court below within the prescribed three years after their discovery of the facts upon which the liability asserted was created.

The fact that appellants have admitted in their statement in brief on appeal that they now have knowledge, obtained subsequent to the time the complaint was filed in this action alleging the sale of the corporate asset subsequent to the date of the

judgment of December 3, 1959, against the corporation, that the conveyance was made in 1954 is, moreover, in no way relevant to their claim against appellees for the wrongful payment of dividends or for the unlawful reduction of the corporation's capital. The wrongful act of the appellees by which they incur statutory liability as directors and shareholders under both sections 1521 and 1804 is, again, their distribution of the proceeds of the sale between them, i.e., their conversion to their own use of the money belonging to the corporation. Appellants have not yet discovered when such distribution was made.

The facts now of record do not establish that this action is barred by section 261 of the Puerto Rico Civil Code or by section 359 of the California Civil Code. Again, appellants still do not know when the distribution of the corporate assets, the proceeds from the sale of the M/V LEDA I, was made by appellees. These facts remain for discovery by the appellants, and it is for the pleading as an affirmative defense by appellees and determination by the trial Court if the unlawful dividend was paid more than six years preceding the filing of the complaint below, and thus the period of liability created by section 1521 of the Puerto Rico Corporation Law has expired, or if the aggrieved parties, the appellants, discovered the facts upon which the statutory liability of appellees as directors or stockholders of the corporation was created more than three years prior to December 3, 1962.

Cf., Hospelhorn v. Newhoff, 43 Cal.App.2d 678, 111 P.2d 688 (1941).

3. APPELLEES MAY BE HELD LIABLE FOR THE JUDGMENT DEBT OF THE CORPORATION WHEN THE CORPORATION IS MERELY THEIR "ALTER EGO".

This is not, as appellees insistently maintain, essentially or excusively a suit "upon the judgment itself" (Appellees' Brief, p. 10). This is an action in which appellants, as creditors of the corporation who happen to be *judgment* creditors of the corporation, seek to recover the amount of a judgment *debt* owed by the corporation to appellants and which the corporation is unable to satisfy due to the wrongful conduct of appellees and for which they are liable by virtue of statutory provisions and common law principles.

Nor is this an action against the appellees for the corporate tort which resulted in the wrongful death of appellants' father. Appellees are liable for their wrongful acts which rendered the corporation insolvent and unable to pay its judgment debt. They are therefore liable to appellants as judgment creditors under sections 1521 and 1804 of the Puerto Rico Corporation Law (Appellants' Opening Brief, pp. 20-23) and under the common law liability of directors for the wrongful distribution of assets rendering the corporation insolvent or of directors and shareholders who have received such assets impressed with a trust in favor of creditors (Appellants' Opening Brief, pp. 17-18).

Appellants do advance as an alternate theory, in support of their contention that it does not appear to a certainty that the appellants would not be entitled to relief under any set of facts which could be proved in support of the claim pleaded and therefore the

complaint should not have been dismissed (Appellants' Opening Brief, pp. 12, 14), that the corporate entity of Snow Lines, Inc., should be disregarded and appellees should be held personally liable *on the judgment* against the corporation (Appellants' Opening Brief, pp. 25-28).

Appellees have ignored appellants' citation at page 26-28 of their Opening Brief of the case of *Cruz v. Ramirez,* 75 P.R.R. 889, 895-96 (1954), in which the Supreme Court of Puerto Rico held that a complaint seeking to enforce a judgment debt of a corporation against individual stockholders, on the theory that the corporation was the mere "alter ego" of those stockholders, was not subject to dismissal but stated sufficient facts to furnish the trial Court a basis for deciding whether the circumstances of the particular case warranted the application of the "alter ego" rule in enforcing the judgment against the stockholders.

The only authority cited in appellees' argument for the proposition that individuals may not be held liable for judgments against their corporate alter egos is *Minton v. Cavaney,* 56 Cal.2d 576, 364 P.2d 473 (1961). Appellants maintain that this case stands, rather, by implication, for the opposite proposition. Plaintiffs in that action sought to hold the defendant personally liable for a judgment recovered against a corporation for the wrongful death of plaintiffs' daughter. The defendant died while the action was pending and prior to trial and his executrix was substituted as defendant. In its opinion the California

Supreme Court recited the various situations which are an abuse of the corporate privilege and to which the "alter ego" or "disregard of the corporate entity" theory will therefore apply. These included situations in which the owners of the corporation treat the assets of the corporation as their own and add or withdraw capital from the corporation at will, and situations in which they provide inadequate capitalization and participate actively in the conduct of corporate affairs. 364 P.2d at 475, and authorities cited therein.

The Court characterized the action as one "to hold defendant . . . personally liable for the judgment against . . . [the corporation]." 364 P.2d at 474, 476. The Court did not hold that such an action could not be maintained or that the "alter ego" doctrine would not apply, but held merely that a corporate director would not be held personally liable upon a judgment against the corporation for negligence, when the defendant director had neither been a party to the action against the corporation nor had he controlled the litigation leading to the judgment against the corporation, without an opportunity to relitigate the issues of the corporation's negligence and the amount of damages, and in that case the plaintiff had failed to allege or present any evidence on the issue of the corporation's negligence or the amount of damages. 364 P.2d at 476.

In the complaint filed below in this action, it is alleged that "by reason of the negligence" of the corporation, the plaintiff's father suffered injuries which resulted in his death, as a result of which "plaintiffs

. . . suffered damages in the sum of Twenty Thousand Dollars ($20,000)" (Tr. 3), and further evidence would be presented to support those allegations of the corporation's negligence and the amount of damages. Appellees would have the opportunity to assert in this action any defense against those allegations that they might have raised in the earlier action.

Section 2202(b), Chapter 112, Title 14, Private Corporations, 3A Laws of Puerto Rico (1962), expressly provides that when a suit is brought against an officer, director or shareholder of a corporation for a debt or liability of the corporation and after judgment has been obtained therefor against the corporation, "any such officer, director or stockholder may set up any defense which the corporation might have asserted against such debt or liability."

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4. **APPELLANTS ARE NOT COLLATERALLY ESTOPPED FROM ASSERTING THAT THE CORPORATION IS THE ALTER EGO OF THE APPELLEES.**

In *Minton v. Cavaney, supra,* furthermore, the same plaintiffs who sought to enforce personal liability upon the defendant director for the judgment against the corporation had brought the prior action against the corporation, asserting that the corporation was in existence and duly incorporated in California. The corporation, which had operated a pool in which the plaintiffs' child had drowned, was specifically found by the Supreme Court to have been duly incorporated in California and its existence had never been for-

mally dissolved. The plaintiffs were not, however, "collaterally estopped" from asserting that the corporation was defendant's "alter ego" for purposes of holding him personally liable for the corporate judgment debt. The Court held, rather, that the judgment against the corporation in no way barred the action against the individual defendant based entirely upon the "alter ego" doctrine. 364 P.2d at 476. Nor do we find any other authority in support of the theory of collateral estoppel under such circumstances as advanced by the appellees in their brief at pages 5, 11-12.

Moreover, as pointed out above, any such rule of collateral estoppel would bar only the appellants' denial of the corporation's valid existence prior to the date of the Judgment of December 3, 1959, and not a denial of its existence subsequent to that time when it is alleged the appellees' personal liability arose.

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5. THE COMMON LAW THEORY OF LIABILITY OF DIRECTORS AND SHAREHOLDERS OF A CORPORATION TO CREDITORS FOR THE DEBTS OF THE CORPORATION IS RECOGNIZED BY THE SUPREME COURT OF PUERTO RICO.

The common law theory of liability of directors and shareholders who have received a distribution of corporate assets to creditors and all others holding claims, asserted by appellants in their Opening Brief at page 18, has been expressly enunciated, contrary to appellees' contention at pages 13-14 of their brief, by the Supreme Court of Puerto Rico in the case of

Cruz v. Ramirez, 75 P.R.R. 889, 895 (1954), as follows:

> "The creditors of a corporation may personally sue the stockholders or the directors who are constituted trustees in liquidation after dissolution, with respect to the property of the corporation held by those stockholders or trustees, and if the latter dispose of, or sell that property to the prejudice of creditors, they may incur a personal liability to those creditors. Fletcher, *Cyclopedia of the Law of Private Corporations*, Vol. 16, § 8161, p. 922 *et seq.; Koch v. U.S.*, 138 F.2d 850; *Hutton v. Commissioner of Internal Revenue*, 59 F.2d 66, particularly if the corporation is insolvent after dissolution. *Cf.* 13 Am. Jur. 991. The relevant rule is to the effect that such property should be considered as existing for the benefit, in part, of the creditors, and such stockholders or trustees receive it, in part, for the benefit of the creditors, and therefore they may not dispose of such property to the creditors' prejudice. Regarding the 'trust-fund' rule as respects such property, see 13 Am.Jur. 1197.
>
> "It is alleged in the complaint before us that the defendants have sold the property of the corporation and have rendered it insolvent to the prejudice of plaintiffs as creditors, 'for the sole and deliberate purpose of defrauding the plaintiffs as creditors.' Such allegation is sufficient to hold defendants personally liable, in view of the rules set forth above."

6. APPELLANTS' ACTION AS BASED UPON COMMON LAW DOCTRINES WAS FILED IN THE COURT BELOW WITHIN THE APPROPRIATE PERIOD OF LIMITATIONS.

It was pointed out above that section 261 of the Pureto Rico Code of Civil Procedure does not bar the appellants' action under the statutory or common law theories of appellees' liability advanced by appellants.

Appellees argue at pages 14-15 of their brief that a cause of action based upon the common law doctrine, as clearly accepted by the Supreme Court of Puerto Rico in *Cruz v. Ramirez, supra*, would be barred by the statute of limitations, citing as the applicable statute section 5298 of the Puerto Rico Civil Code. This section provides a one-year limitation period for actions arising under section 5141 of the Civil Code, which reads as follows:

> "§ 5141. A person who by an act or omission causes damage to another when there is fault or negligence shall be obliged to repair the damage so done." Chapter 393, Title 31, 8 Laws of Puerto Rico (1955).

Appellees further assert that the action would also be prescribed under section 361 of the California Code of Civil Procedure which provides that a cause of action is barred in California when it would be barred by the statute of limitations of the state or foreign country where the cause of action arose.

Appellants concede that appellees have chosen that statutory provision in section 5141 which apparently encompasses the fraudulent conduct of appellees and

that an action against them might be barred under section 5298 of the Puerto Rico Civil Code were it not that the prescription statute was tolled and has not run against the appellants.

Appellants alleged in their memorandum submitted to the Court below (Tr. 47) and in their Opening Brief at page 4 that appellees left the Commonwealth of Puerto Rico in 1954. It is unknown to appellants and therefore subject to discovery in this action or affirmative plea by appellees, whether appellees have ever returned to the Commonwealth of Puerto Rico or for what periods of time they have done so.

Section 253 of the Puerto Rico Code of Civil Procedure, Chapter 41, Title 32, 8 Laws of Puerto Rico (1955) provides as follows:

> "If when the cause of action accrues against a person, he is out of the Commonwealth of Puerto Rico, the action may be commenced within the term herein limited after his return to said Commonwealth, and if, after the cause of action accrues, he departs from said Commonwealth, the time of his absence is not part of the time limited for the commencement of the action."

Section 254 of the Puerto Rico Code of Civil Procedure provides in relevant part as follows:

> "§ 254. If a person entitled to bring an action, other than for the recovery of real property, be at the time the cause of action accrued, either:
>
> 1. Within the age of majority; . . .
>
> the time of such disability is not a part of the time limited for the commencement of the action."

The above-quoted section 254 is derived from and its language is essentially identical to section 352 of the California Code of Civil Procedure.

The action insofar as it is based upon the common law is therefore not barred by the Puerto Rican prescription statute cited by appellees or under section 361 of the California Code of Civil Procedure.

Nor is the action barred by section 338 of the California Code of Civil Procedure which imposes a three-year period of limitation for an action for relief on the ground of fraud. This statute is likewise tolled by section 352 of the California Code of Civil Procedure during the minority of the appellants.

The complaint filed below affirmatively shows that appellants, plaintiffs below, are minors (Tr. 1, 3) and the suit was brought on their behalf by their next friend, and it is clear that the cause of action accrued to the minor appellants themselves and that therefore the statute of limitations was tolled during their minority.

Aronson v. Bank of America N.T. & S.A., 42 Cal.App.2d 710, 109 P.2d 1001, 1007 (1941).

Section 338 provides, moreover, that an action subject to the three year limitation period for actions based on fraud is not "deemed to have accrued until the discovery, by the aggrieved party, of the facts constituting the fraud."

As appellants have alleged above, the fraudulent conduct of appellees was not discovered by them until after they had obtained the judgment against the

corporation, execution on which was returned unsatisfied because of the corporation's insolvency. This action was, therefore, instituted within the three year limitation period prescribed by section 338 of the California Code of Civil Procedure.

Under appellants' theory that the appellees should be held personally liable for the judgment against their corporate "alter ego," the applicable statute of limitations is section 337.5 of the California Code of Civil Procedure, prescribing a ten year period for actions upon judgments or decrees of any Court of the United States. This action was instituted within three years of the time their action accrued based upon the judgment rendered December 3, 1959, by the District Court of Puerto Rico.

Dated, Oakland, California,
January 17, 1964.

Respectfully submitted,

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No. 18836

In the United States Court of Appeals for the Ninth Circuit

UNITED STATES OF AMERICA, APPELLANT

v.

WILLIAM LUCIAN COBB, ET AL., APPELLEES

Appeal From The United States District Court For The Northern District of California

BRIEF FOR THE UNITED STATES, APPELLANT, OR IN SUPPORT OF ALTERNATIVE PETITION FOR WRIT OF MANDAMUS OR PROHIBITION

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UNITED STATES OF AMERICA, APPELLANT

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Appeal From The United States District Court For The Northern District of California

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BRIEF FOR THE UNITED STATES, APPELLANT, OR IN SUPPORT OF ALTERNATIVE PETITION FOR WRIT OF MANDAMUS OR PROHIBITION

OPINIONS BELOW

The district court entered unreported memorandums and orders in this case on May 18, 1962, August 8, 1962, and March 14, 1963 (R. 50, 64, 71).

JURISDICTION

The district court had jurisdiction over the condemnation proceeding instituted by the United States under 28 U.S.C. sec. 1358. The order of the district

court denying the Government's motion for an order of immediate possession and vacating and setting aside the declaration of taking was entered on March 14, 1963. The notice of appeal from this final order was filed on May 13, 1963. This Court has jurisdiction over the appeal under 28 U.S.C. sec. 1291. This Court has jurisdiction under 28 U.S.C. sec. 1651(a) to issue a writ of mandamus or prohibition.

QUESTIONS PRESENTED

1. Whether the district court has authority to dismiss a declaration of taking filed by appropriate officials of the executive department pursuant to 40 U.S.C. secs. 258a-258f, after the sum estimated by the acquiring agency to be just compensation has been deposited with the court.

2. Whether the district court has authority to dismiss a declaration of taking, which is otherwise regular, because of an alleged lack of good faith on the part of the proper administrative authorities in estimating just compensation.

STATEMENT

The United States, on October 23, 1961, filed its complaint and declaration of taking to take such easements and rights of way, if any, as the United States did not already have, to use, reconstruct, improve and maintain the existing Elliott Creek Road No. 193, and to construct, reconstruct, use, improve and maintain the proposed Dutch Creek Road No. 193A (R. 4). The estates and interests set out in the complaint

were over and upon unpatented mining claims within public domain lands reserved and administered as part of the Rogue River National Forest in Siskiyou County, California (R. 4, 21). Since the commencement of the suit, a patent has been issued on one of the mining claims (R. 72). This patent was issued subject to the declaration of taking involved here (*Ibid.*). The complaint and declaration of taking covered also the right to reconstruct, use, improve and maintain any segment of the roads destroyed through mining operations, and the right to construct, use, improve and maintain in such manner as will not materially interfere with mining operations such temporary bypass roads during mining operations as are made necessary by the destruction of the roads (R. 4, 22).

The complaint and declaration of taking reserved to the owners of valid mining claims the right to conduct mining operations on the lands described, including the right to destroy the existing Elliott Creek Road No. 193, the proposed Dutch Creek Road No. 193A, and temporary bypass roads where the owners deem the destruction necessary to the exercise of the mining operations (R. 4, 22). To the owners of valid mining claims was also reserved the right to use these roads and cross on, over or underneath them in such manner as would not endanger the road (R. 5, 23). The sum estimated as just compensation for the taking of the estate and interests described in the declaration of taking was $1.00, which was deposited (R. 23).

The appellees W. L. Cobb, *et al.*, filed an answer and subsequently an amended answer in which they challenged the taking on the ground that (1) it was not for a public use, (2) it was not authorized by law, and (3) the declaration of taking should be stricken because the estimate of just compensation was not made in good faith (R. 37, 42). The amended answer alleged the taking was not for a public use on the following basis (R. 43-44). In January 1956, Bate Lumber Company and others entered into a contract with the United States Department of Agriculture, Forest Service, wherein Bate agreed to construct Elliott Creek Road No. 193 and Dutch Creek Road No. 193A. Bate agreed to acquire the easements for the road right of way across all mining claims traversed. Bate has not acquired such easements, and it is alleged that the United States in this proceeding is attempting to fulfill the contractual obligation of Bate. The amended answer alleged that the condemnation proceeding was not authorized by law because no appropriation had been made, and because the easement sought was too vague (R. 44).

Finally, it was alleged that the deposit with the declaration of taking was not made in good faith, that a reasonable estimate of just compensation would be in excess of one million dollars for the reason that the 21 mining claims of the appellees will be bisected by the road easements which will render it economically impractical for the appellees to operate their claims (R. 44-45.).

The United States filed a motion to strike the amended answer, grant judgment on the pleadings

and issue an order of possession (R. 48). After memorandums in support of and in opposition to the Government's motion had been submitted, the district court entered its order and memorandum of May 18, 1962. The court held that the estate described in the complaint and declaration of taking was sufficiently specific (R. 51-52). The court held that the use was a public one, and the fact that the road was to be built by a private owner under agreement with the Government does not change the public purpose (R. 53-54). However, the court found that it had the power and duty to determine whether the amount of the deposit was in fact an estimate of just compensation arrived at in good faith (R. 54-56). The court thought the issue should have been raised by an independent motion to dismiss the complaint and declaration of taking, rather than in the answer (R. 56). Accordingly, the district court ordered paragraphs 3, 4 and 5 of the amended answer stricken, and granted the Government's motion to deny the demand in the answer that the complaint and declaration of taking be dismissed (R. 56-57). The Government's demand for judgment on the pleadings and for immediate possession was denied (R. 57).

Appellees thereafter filed their motion to dismiss the complaint and declaration of taking (R. 58-61). The Government filed a motion to reconsider or, in the alternative, for an interlocutory appeal (R. 62). After further briefing, the district court entered its order of August 8, 1962 (R. 64). On reconsideration, the district court decided that the appellees' motion

to dismiss the complaint was properly a part of the answer, and reinstated paragraph 5 of the amended answer which had previously been stricken (R. 65). The court reiterated its previous position that it had jurisdiction to inquire into the issue of good faith in the estimate of the deposit (R. 66 *et seq.*). The Government's motion for an interlocutory appeal was denied (R. 67).

The hearing before the district court on the good faith issue was held on December 17, 1962. At that hearing the Government, after re-emphasizing its position that the court was without jurisdiction to hear evidence on the issue, presented Mr. Milvoy Suchy, a mining engineer with the Department of Agriculture (R. 91-137). Mr. Suchy graduated from the Colorado School of Mines in 1938 and has been actively engaged in mining or closely related fields since then except for two and one-half years during the war (R. 92-93). He has been acquainted with the appellees' placer mining claims since 1957 (R. 94). The Elliott Creek Road was in existence at that time (R. 96). It was a private road which had been built by Bate Lumber Co. (R. 97). Mr. Suchy made a report with reference to the present condemnation proceeding about these mining claims in the first part of 1961 (R. 98). He was advised that the Government intended to condemn a road right of way over these mining claims (*Ibid.*). It was his understanding that the land was owned by the Government as part of the national forest on which there were certain rights outstanding in the form of mining claims (R. 99). The Government was trying to get the right

to use the road which had already been built across these mining claims (*Ibid.*)

Mr. Suchy related the circumstances under which the road had been built. The Bate Lumber Company had obtained an easement across the Rogue River National Forest, subject to all valid mining claims (*Ibid.*). It had proceeded to obtain easements across the mining claims, but they were obtained from the wrong party and the road built on that basis (*Ibid.*). The appellees had then commenced a suit in Siskiyou Superior Court against Bate for trespassing damages and recovered $10,000 (R. 99-100). This testimony was later withdrawn, but the parties agreed that there was a suit brought and certain damages were awarded along with a permanent injunction against Bate Lumber Company (R. 102).

Mr. Suchy had examined the declaration of taking and his understanding of the estate to be taken in this case was as set forth in it (*Ibid.*). Mr. Suchy then produced the report dated January 23, 1961, giving his opinion as to what damages, if any, would be done to the appellees' mining claims by virtue of the taking described (R. 103). This was introduced as Plaintiff's Exhibit 3 (R. 104). In this report, Mr. Suchy concluded that appellees' mining rights would not be damaged by this interruptable type easement (R. 104).

There was next introduced in evidence as Plaintiff's Exhibit No. 4 a letter dated October 4, 1961, from the Secretary of Agriculture to the Attorney General, conveying the initial documents for the condemnation proceeding and setting forth the reason for the deposit of $1.00 as estimated just compensation (R.

105). With this evidence, the Government completed its showing of a prima facie compliance with the declaration of taking procedures.

On cross-examination it was developed that Mr. Suchy did not assign any dollar value to the claims (R. 107). He did not believe there would be any damages for the easements which the Government was now taking because the owners of the claims had been paid $10,000 by the judgment in the Superior Court of California for Siskiyou County (R. 107). That amount had been paid entirely by Bate, the Government not being a party to that proceeding (R. 108). If Mr. Suchy's assumption that all damages were paid for by the $10,000 judgment in Superior Court were erroneous, then he would say his report was wrong (R. 109). Under questioning from the district court, Mr. Suchy gave the following as the basis for his estimate of damage (R. 114):

> A. When I examined the mining claim, sir, I went there with the idea of determing [sic] what damage would be done to the claimant in his mining operation if he was allowed to remove the road. It was interruptable type easement. I came to the conclusion that since the material that covers his placer deposit had been the subject of a previous State proceeding and he was awarded $10,000 damages for the removal of this material, it didn't make any difference whether it was removed by, say, a drag line or if he went in there and removed it and then mined it. He could do it either way. As long as the road easement is interruptable he can mine under the road. The material from the

> road, the damage that has been done, has already been paid for, sir.

After some confusion, finally clarified by government counsel, Mr. Suchy was asked by counsel for the appellees (R. 118):

> Q. Now isn't it true that a prospective purchaser, sir, of these two claims would pay less for the claims with an easement for a road across them than what he would pay without such an easement?
>
> A. An interruptable easement which would allow him to mine without being held for damages to the road I don't believe would affect the price materially.

There followed in the cross-examination extensive questioning about the details of Mr. Suchy's report and the mining operations involved on the appellees' mining claims (R. 118-123).

During the course of this cross-examination, government counsel objected to the line of questioning as being argumentative (R. 130). Government counsel then stated (*Ibid.*):

> Again I would like to emphasize, let's assume argumento [sic] that this witness is absolutely wrong in his opinion of value as opposed to the opinion of value of the defendants. That isn't the issue here. The issue is whether or not he submitted an estimate as to the damages of this particular easement to the Secretary of Agriculture and the Secretary of Agriculture had a right to rely thereon.

After further colloquy between counsel and the district court, the district court took the case under submission and asked for further memorandums from counsel (R. 137-146). During this colloquy, the district court commented (R. 141, 142):

> The thing that plagues me is the fact that I cannot conceive in this day and age how anything can be worth only one dollars [sic]. I don't know what you can buy with it. I have just been over to the Philippines, and, of course, the standards over there are so much different from ours. You are a little shocked when you hear that a person receives 30 pesos for a month's labor. That is about $7.50 a month pay. Many families are having to struggle along and live on that.
>
> * * * *
>
> That is what is plaguing me about this matter here. I just can't conceive of anything being worth only a dollars [sic]. That is what bothers me.
>
> If the Government had seen fit to put up $500 or $1,000 I wouldn't even give a second thought to this matter here, I would pass it away immediately; but when they put up a dollar it looks to me like it is really an insult to the defendants in the case.

On March 14, 1963, the district court entered its third and final memorandum and order (R. 71-82). In this memorandum, the district court was of the view "that the requirement of estimated just compensation as the basis for a deposit (as contemplated by § 258a) includes a requirement that such

estimate be made in good faith. I am also of the view that any contention that a bad faith estimate has been made is cognizable before the courts * * *" (R. 73). The court made a distinction between the inquiry into good faith and "an inquiry * * * into the sufficiency of a deposit, which clearly is impermissible * * *" (R. 73). After reviewing the testimony of Mr. Suchy, the district court came to the conclusion that Mr. Suchy's determination of nominal damages was based on erroneous legal assumptions and therefore the deposit was not made in good faith "that is, with a reasonable basis for belief as to its accuracy" (R. 79).

The court then proceeded to examine the question of whether the declaration of taking should be dismissed (R. 79-82). The court was of the opinion that the cases are "in hopeless conflict as to whether a United States District Court has authority to vacate a declaration of taking, where a showing of lack of good faith is made" (R. 80). The district court noted that the Ninth Circuit has indicated no such authority exists "under ordinary circumstances" (*Ibid.*). However, the district court thought an exception could be made where there is "the additional element of a failure to comply with the good faith requirement * * *" (*Ibid.*). Accordingly, the district court vacated and set aside the declaration of taking without prejudice to the Government to file an amended declaration of taking. This appeal followed.

SPECIFICATION OF ERRORS

The errors of the district court are:

1. The Memorandum and Order of March 14, 1963, which ordered the declaration of taking to be set aside and vacated and which denied the United States immediate possession of the property involved (R. 82).

2. The holding of the Memorandum and Order of March 14, 1963, that 40 U.S.C. sec. 258a "includes a requirement that such estimate [of just compensation] be made in good faith" (R. 73). The further holding at the same place that "any contention that a bad faith estimate has been made is cognizable before the courts * * *" (R. 73).

STATUTES INVOLVED

The Act of February 26, 1931, 46 Stat. 1421, 40 U.S.C. secs. 258a-258e, provides:

> *Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That in any proceeding in any court of the United States outside of the District of Columbia which has been or may be instituted by and in the name of and under the authority of the United States for the acquisition of any land or easement or right of way in land for the public use, the petitioner may file in the cause, with the petition or at any time before judgment, a declaration of taking signed by the authority empowered by law to acquire the lands described in the petition, declaring that said lands are thereby taken for the use of the United

States. Said declaration of taking shall contain or have annexed thereto—

(1) A statement of the authority under which and the public use for which said lands are taken.

(2) A description of the lands taken sufficient for the identification thereof.

(3) A statement of the estate or interest in said lands taken for said public use.

(4) A plan showing the lands taken.

(5) A statement of the sum of money estimated by said acquiring authority to be just compensation for the land taken.

Upon the filing said declaration of taking and of the deposit in the court, to the use of the persons entitled thereto, of the amount of the estimated compensation stated in said declaration, title to the said lands in fee simple absolute, or such less estate or interest therein as is specified in said declaration, shall vest in the United States of America, and said lands shall be deemed to be condemned and taken for the use of the United States, and the right to just compensation for the same shall vest in the persons entitled thereto; and said compensation shall be ascertained and awarded in said proceeding and established by judgment therein, and the said judgment shall include, as part of the just compensation awarded, interest at the rate of 6 per centum per annum on the amount finally awarded as the value of the property as of the date of taking, from said date to the date of payment; but interest shall not be allowed on so much thereof as shall have been paid into the court.

No sum so paid into the court shall be charged with commissions or poundage.

Upon the application of the parties in interest, the court may order that the money deposited in the court, or any part thereof, be paid forthwith for or on account of the just compensation to be awarded in said proceeding. If the compensation finally awarded in respect of said lands, or any parcel thereof, shall exceed the amount of the money so received by any person entitled, the court shall enter judgment against the United States for the amount of the deficiency.

Upon the filing of a declaration of taking, the court shall have power to fix the time within which and the terms upon which the parties in possession shall be required to surrender possession to the petitioner. The court shall have power to make such orders in respect of encumbrances, liens, rents, taxes, assessments, insurance, and other charges, if any, as shall be just and equitable.

Sec. 2. No appeal in any such cause nor any bond or undertaking given therein shall operate to prevent or delay the vesting of title to such lands in the United States.

Sec. 3. Action under this statute irrevocably committing the United States to the payment of the ultimate award shall not be taken unless the chief of the executive department or agency or bureau of the Government empowered to acquire the land shall be of the opinion that the ultimate award probably will be within any limits prescribed by Congress on the price to be paid.

Sec. 4. The right to take possession and title in advance of final judgment in condemnation proceedings as provided by this Act shall be in addition to any right, power, or authority conferred by the laws of the United States or those of any State or Territory under which such proceedings may be conducted, and shall not be construed as abrogating, limiting, or modifying any such right, power, or authority.

Sec. 5. In any case in which the United States has taken or may take possession of any real property during the course of condemnation proceedings and in advance of final judgment therein and the United States has become irrevocably committed to pay the amount ultimately to be awarded as compensation, it shall be lawful to expend moneys duly appropriated for that purpose in demolishing existing structures on said land and in erecting public buildings or public works thereon, notwithstanding the provisions of section 355 of the Revised Statutes of the United States: *Provided,* That in the opinion of the Attorney General, the title has been vested in the United States or all persons having an interest therein have been made parties to such proceeding and will be bound by the final judgment therein.

The Act of October 21, 1942, 56 Stat. 797, 40 U.S.C. sec. 258f, provides:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That in any condemnation proceeding instituted by or on behalf of the United States, the Attorney General is au-

thorized to stipulate or agree in behalf of the United States to exclude any property or any part thereof, or any interest therein, that may have been, or may be, taken by or on behalf of the United States by declaration of taking or otherwise.

SUMMARY OF ARGUMENT

Introductory.— Before the broad legal issues in this case are discussed, it will be helpful to note the precise factual background of the case. The "bad faith" which the district court found was, in substance, that the fully qualified mining engineer whom the Secretary of Agriculture had chosen to make an estimate of damages took into account the fact that an existing road was being condemned and damage caused by its construction had been paid by Bate Lumber Company. This was a fact which the district court did not think should be considered in estimating just compensation. The decided cases suggest that "bad faith" is the equivalent of "fraudulent action" or "actual malevolence or spite" and not merely poor judgment or careless planning. But the strongest case against the Government would be a charge that it erroneously interpreted unsettled law. There is nothing to show that governmental officials were motivated by fraud, malice or personal ill will against the appellees.

As in all cases where there is alleged to be a lack of good faith, it is simply the refusal of the district court to agree with the economic and legal result reached by the administrative officials. The district court cannot so substitute its judgment for that of the

responsible administrative officials. It is apparent that the district court was chiefly disturbed by the fact that only one dollar was deposited. The United States may use a condemnation suit to effect a quiet title. The nominal deposit is simply an assertion that the United States already owns the property right described in the complaint and declaration of taking except for mere technical rights outstanding.

I

The district court has no jurisdiction to dismiss a declaration of taking. When the United States filed its declaration of taking and deposited estimated just compensation, title to the estate described vested in the Government. Thereafter, the district court is powerless to dismiss the proceeding or the declaration of taking. The district court indicated that it was cognizant of that rule as stated in the cited decisions of this Circuit. The district court proceeds to find an exception, however, "where a showing of lack of good faith is made." It has already been noted that no showing of bad faith by government officials has been made in this case. Moreover, as will be shown, the "bad faith" exception which the district court purported to find does not exist at all.

II

The allegation of the defendant in a condemnation suit that the estimate of just compensation for a declaration of taking has been made in bad faith does not present a justiciable issue. There is no conflict of authorities on this point, and no final decision which

supports the district court's asserted jurisdiction. To the contrary, the Fifth Circuit has ruled that the purported bad faith exception to the rule of finality of the administrative estimate of just compensation does not exist. *In re United States*, 257 F.2d 844 (1958). We now show why this decision should be followed by this Court.

"Good faith" and "bad faith" are not statutory standards. The statute simply requires that the acquiring agency deposit estimated compensation with the court. There is no question but that this has been done. The purposes of the Declaration of Taking Act were to give the Government immediate possession and to relieve it of the burden of interest on the sum deposited as estimated compensation. Second, it gives to the former owner, if his title is clear, immediate compensation to the extent of the Government's estimate. The Supreme Court decisions make it clear that the estimate is tentative. The possibility is contemplated that administrative officials may intentionally underestimate the value of property to protect the Government. This view is premised on the administrative estimate being conclusive. Congress gave the acquiring agency, not the courts, the function of estimating compensation for this purpose. The lack of court review is evident from the fact that title changes when the estimated compensation is deposited in court without the necessity of any court order. The delay necessarily resulting from court examination of the deposit in adversary proceedings also demonstrates the lack of juris-

diction for such an undertaking. These time-consuming procedures are directly contrary to the purposes of the statute, which was enacted to prevent delay of government projects by legal proceedings. In providing estimated compensation, Congress was conferring a benefit on the landowner not constitutionally required, as the Government may always seize the land so long as it provides a remedy under the Tucker Act. There is no justification for enlarging the grant to include the power to control the amount of the deposit.

In re United States, supra, refused to imply such power. The Fifth Circuit rejected the view that the district court could vacate a declaration of taking and refuse to give the Government possession. It deemed the settled law to be that the purported bad faith exception to the rule of finality of the administrative estimate of just compensation did not exist. The three cases relied on by the district court for the bad faith exception were either reversed on the ground there is no authority to vacate a declaration of taking or were decided on other grounds with the good faith issue expressly left open.

The district court examined the two leading cases of this Court and other cases holding it is beyond its power to vacate a declaration of taking, and concluded that the cases appear to be in "hopeless conflict." The district court acknowledged that this Court's decision "indicated no such authority exists under ordinary circumstances (i.e., where there is a failure to make a showing of bad faith) * * *." Good faith or bad faith are not discussed by this Court's de-

cisions, nor is any exception intimated to the rule that once title vests by the deposit of estimated compensation the court is powerless to vacate it. The other cases in which the district court purported to find a "hopeless conflict" do not contain a single instance in which the dismissal of a declaration of taking has been sustained.

III

If the order dismissing the declaration of taking is not an appealable order, it is requested that this brief be treated as in support of a petition for mandamus.

A. The Government believes the order is appealable under the collateral orders doctrine. The deposit of compensation, transfer of title and possession under the Declaration of Taking Act procedure are entirely separate from the issue of just compensation. It therefore falls into that class of orders which finally determine claims of right separate from, and collateral to, the rights asserted in the action, too important to be denied review and too independent of the cause itself to require that appellate consideration be deferred until the whole case is adjudicated. It is recognized that this is a close question, but a distinction must be made between this case, where the declaration of taking was dismissed, and those cases where it is held valid. While the order dismissing an action is final and appealable, one that refuses to dismiss is not.

B. In any event, the district court's order dismissing the declaration of taking may be properly re-

viewed by this Court by writ of mandamus or prohibition. The matter at issue is the Government's right of possession pending the determination of just compensation. Once compensation has been determined, the right of possession will become moot. Therefore, appeal is an inadequate remedy. An even stronger reason for mandamus is that the district court ruled on a matter beyond its jurisdiction. The historic use of the writs of mandamus and prohibition has been to confine the inferior court to the lawful exercise of its prescribed jurisdiction. The authority of this Court in the matter is not confined to writs in aid of a jurisdiction already acquired but extends to those cases which are within its appellate jurisdiction, although no appeal has been perfected.

ARGUMENT

Introductory.—This case raises broad legal issues as to the jurisdiction of the district court to dismiss a declaration of taking and the justiciability of the alleged "bad faith" exception to the general rule which the district court purported to find. However, before we begin discussion of these legal issues, and especially of the "bad faith" exception, it will be helpful to note the precise factual background of the case. The "bad faith" which the district court found is set out in its memorandum of March 14, 1963, as follows (R. 78-79):

> Mr. Suchy's examination of the instant property was aimed at determining what damage would be caused to the property by the easement

herein. His assessment that no damage would occur was based upon the supposition that whatever damage the road might cause had already been paid. In view of the fact that the easement herein would permit the Government to completely change the nature of the roads involved, this supposition seems patently erroneous. Mr. Suchy himself came close to admitting as much, in his statement that his report, based upon the above assumption, would be incorrect if such an assumption were incorrect.[1]

It thus appears that Mr. Suchy's determination that the easement herein would cause only nominal damage to the mining claims was based upon a clearly erroneous legal assumption as to the effect of the judgment against Bates Lumber Co. In view of said error, it follows that the report submitted by him to the Department of Agriculture was so defective as to amount to a mere guess as to the decrease in value to follow from the proposed easement herein. Under such a set of circumstances, it cannot be said that the estimate by the Department of Agriculture that

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[1] (Appellant's footnote) The Government does not agree that Mr. Suchy's testimony was made on the basis of an incorrect assumption. Reading the record as a whole, we believe that the fair interpretation of Mr. Suchy's testimony was that he estimated damages on the basis of the road, including all the fill dirt necessary for its construction, already being in place over the mining claims (see especially R. 113-114). That the fill dirt and road were already on the mining claims is an undisputed fact. It is immaterial that Mr. Suchy may have expressed himself inaptly in speaking in terms of the Bate Company damage suit rather than the actual condition of the property as he found it. We do not pursue this matter, however, since in our view it is simply another tangent to the real issue in the case.

> just compensation for the taking of the easement would be $1 was made in good faith, that is, with a reasonable basis for belief as to its accuracy.

In substance, Mr. Suchy, the fully qualified mining engineer whom the Secretary of Agriculture had chosen to make an estimate of damages, took into account a fact which the district court did not think should be considered in estimating just compensation. This Court in a condemnation proceeding has equated "bad faith" with "fraudulent action." *Simmonds* v. *United States*, 199 F.2d 305, 306-307 (C.A. 9, 1952). Taking the strongest case that possibly could be made under any view of the facts against the Government, at most it could be charged with an erroneous interpretation of law. But, "It [bad faith] does not mean merely poor judgment or careless planning," but rather "actual malevolence, or spite" directed toward the condemnee. *United States* v. *40.75 Acres of Land in DuPage County, Ill.*, 76 F. Supp. 239, 249 (N.D. Ill. 1948). Thus, as noted by the court in *United States* v. *Southerly Portion of Bodie Island, N.C.*, 114 F.Supp. 427, 430 (E.D. N.C. 1953): "To allege bad faith a party must charge facts rather than conclusions, and such facts must suggest actual malevolence by the officer towards the complaining party." And, of course, even if there were something in the present case which remotely resembled such "bad faith," it would have to be proved—a matter which, like fraud, must be established by clear and convincing evidence.

There is no hint that Mr. Suchy or the Department of Agriculture officials who relied on his report were motivated by fraud, malice or personal ill will against the appellees. No chicanery or connivance is shown in the evidence. There is not the slightest indication that the government officials intended to cheat the appellees out of the fair market value of their claims. Nor is there any intimation that deception was practiced on the appellees.

To the extent that fair market value might be underestimated, whether the legal or economic theories are the causative factor, the disadvantage is with the United States. The Government must pay 6% interest on the deficiency from the date of taking until the date compensation is finally paid. Act of February 26, 1931, 46 Stat. 1421, 40 U.S.C. sec. 258a. The Government can borrow money at interest rates considerably below 6%. It is clearly not to the Government's economic advantage to underestimate just compensation. As in all the cases where there is alleged to be a lack of good faith, it is simply a refusal of the district court to agree with the economic and legal result reached by the administrative officials. In effect, as the Fifth Circuit noted in *In re United States*, 257 F.2d 844, 848 (1958), cert. den., 358 U.S. 908, the district court, under the guise of a good faith test, imposes its financial judgment on the administrative officials. If the administrative officials disagree with the court's financial judgment, they must either not use the declaration of taking procedure at all, or submit an estimate of just compensation in which they do not believe. This Circuit

has previously held that the district court cannot so substitute its judgment for that of the responsible administrative officials. *United States* v. *Merchants Transfer & Storage Co.*, 144 F.2d 324, 326 (1944). The only alternative to such an estimate of just compensation in which the administrative official did not believe would be physical seizure. No purpose would be served by forcing the United States to abandon its orderly procedure in favor of physical seizure. *Best* v. *Humboldt Placer Mining Co.*, 371 U.S. 334, 340 (1963).

It is apparent from the district judge's comments at the hearing of December 17, 1962, that the court was disturbed chiefly by the fact that only one dollar had been deposited (R. 141-142). The court was incredulous that anything these days could be worth only one dollar (R. 141). Accordingly, the United States emphasizes what it believes to be evident. The United States may use a condemnation proceeding to effect a quiet title. *United States* v. *93.970 Acres*, 360 U.S. 328 (1959). The nominal deposit of one dollar is simply an assertion that the United States already owns the property right described in the complaint and declaration of taking except for mere technical rights outstanding which have only a nominal value, if any. Even where the Government doesn't own the underlying fee, the compensation may be only nominal. *State of Washington* v. *United States*, 214 F.2d 33 (C.A. 9, 1954), cert. den., 348 U.S. 862; *Terminal Coal Co.* v. *United States*, 172 F.2d 113 (C.A. 3, 1949). See also *United States* v. *16*

Parcels of Land in City of St. Louis, 281 F.2d 271 (C.A. 8, 1960). Therefore, even if the "good faith" or "bad faith" of the proper administrative officials were a legitimate issue, the fact that there was a deposit of nominal compensation would not of itself be a determinative factor in deciding the issue. We now turn to the precise legal issues involved.

I

The District Court Has No Jurisdiction To Dismiss A Declaration of Taking

When, pursuant to the provisions of the Act of February 26, 1931, 46 Stat. 1421, 40 U.S.C. sec. 258a-258f, the United States filed the declaration of taking and deposited the estimated compensation in the registry of the district court, title to the estate described in the declaration of taking vested in the United States. *United States* v. *Carey,* 143 F.2d 445, 450 (C.A. 9, 1944). Upon the filing of the declaration of taking and the passing of title to the Government, the district court is powerless to dismiss the proceeding.[2] *United States* v. *Hayes,* 172 F.2d 677, 679 (C.A. 9, 1949), and cases there cited. *A fortiori,* the district court is powerless to dismiss the declaration of taking.

The Declaration of Taking Act enables the United States to acquire title simply by depositing funds "for or on account" of just compensation to be award-

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[2] This assumes that the taking is authorized by a statute valid under the Constitution. *Catlin* v. *United States,* 324 U.S. 229 (1945).

ed the owners rather than by making payment pursuant to court order. *United States* v. *Dow*, 357 U.S. 17, 23 (1958). The scheme of the Declaration of Taking Act makes it plain that, when the Government files a declaration before it has entered into possession of the property, the filing constitutes the "taking" (*Ibid.*). The court does not award the right of possession nor adjudge the title. The Declaration of Taking Act gives the right of possession, without the necessity of any court order, though it is orderly to get one.[3] *In re United States*, 257 F.2d 844, 846 (C.A. 5, 1958), cert. den., 358 U.S. 908. Cf. *United States* v. *Merchants Transfer & Storage Co.*, 144 F. 2d 324 (C.A. 9, 1944).

This interpretation of the Declaration of Taking Act is entirely consistent with the overall scheme of the federal taking of property. Broadly speaking, the United States may take property pursuant to its power of eminent domain in one of two ways: It can enter into physical possession of property without authority of a court order; or it can institute condemnation proceedings under various acts of Congress providing authority for such takings. *United States* v. *Dow*, 357 U.S. 17, 21 (1958). Under the first method—physicial seizure—no condemnation proceeding is instituted and the property owner is provided a remedy under the Tucker Act, 28 U.S.C. secs. 1346(a)(2) and 1491, to recover just compensation.

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[3] The Act authorizes the court to fix the time for possession (40 U.S.C. sec. 258a) but, since the right to possession follows title, this merely covers a reasonable time for moving out.

Under the second procedure, the Government can wait until just compensation is judicially determined before it pays the award and enters possession, thereby taking the land. Or it can acquire title and right of possession before just compensation has been judicially determined by filing the declaration of taking and depositing just compensation under the Declaration of Taking Act (*Ibid.*).

We shall not belabor the general rule that, when the United States files the declaration of taking and deposits estimated just compensation, title passes from the landowner to the Government, and that, where there is authority for the taking, the district court is thereafter powerless to deprive the Government of its title and revest it in the landowner except as Congress may by statute provide. The district court's opinion of March 14, 1963, indicates that it was cognizant of the general rule as announced in the above-cited decisions of this Circuit (R. 80). The district court proceeds further, however, to find an exception "where a showing of lack of good faith is made" (*Ibid.*). It has already been noted in the introductory remarks of this brief that there has been no showing of bad faith by government officials in the particular facts of this case. We shall now examine what is more basic, that the "bad faith" exception as to the deposit which the district court purported to find in the decided cases does not exist at all.

II

The Allegation Of The Defendant In A Condemnation Suit That The Estimate Of Just Compensation For A Declaration Of Taking Has Been Made In Bad Faith Does Not Present A Justiciable Issue

As a matter of authorities, there is not, as the district court conceived it, a conflict of decision. As we spell out later herein, there is, in our view, no final decision which supports the district court's asserted jurisdiction to review adminstrative action. On the contrary, the Fifth Circuit has ruled on this precise point that the purported bad faith exception to the rule of finality of the administrative estimate of just compensation does not exist and that a trial court has no jurisdiction to set aside a declaration of taking or to deny possession because it concludes that the deposit is inadequate. *In re United States*, 257 F.2d 844 (C.A. 5, 1958), cert. den., 358 U.S. 908. We now analyze the reason why we believe this decision is clearly correct and should be followed by this Court.

"Good faith" and "bad faith" are not statutory standards. The Declaration of Taking Act says nothing about the "good faith" or the "bad faith" of the acquiring agency in estimating just compensation. The language of the statute is that "Said declaration of taking shall contain * * * (5) A statement of the sum of money estimated by said acquiring authority to be just compensation for the land taken." Therefore, the question is simply whether the acquiring agency has included in the declaration of taking

a statement of the sum estimated to be just compensation. There is no question but that this has been done.

The nature and purposes of the Declaration of Taking Act were described as follows in *United States* v. *Miller*, 317 U.S. 369, 381 (1943):

> The purpose of the statute is two-fold. First, to give the Government immediate possession of the property and to relieve it of the burden of interest accruing on the sum deposited from the date of taking to the date of judgment in the eminent domain proceeding. Secondly, to give the former owner, if his title is clear, immediate cash compensation to the extent of the Government's estimate of the value of the property. The Act recognizes that there may be an error in the estimate, and appropriately provides that, if the judgment ultimately awarded shall be in excess of the amount deposited, the owner shall recover the excess with interest. * * *

The *Miller* case rejected the argument that the United States might not recover back the excess of the deposit above the final verdict. The Supreme Court said (p. 381):

> The payment is of estimated compensation; it is intended as a provisional and not a final settlement with the owner; it is a payment "on account of" compensation and not a final settlement of the amount due. To hold otherwise would defeat the policy of the statute and work injustice; would be to encourage federal officials to underestimate the value of the property with the result that the Government would be sad-

> dled with interest on a larger sum from date of taking to final award, and would be to deny the owner the immediate use of cash approximating the value of his land.

The Supreme Court contemplated the possibility that officials would intentionally underestimate the value of the property to protect the Government. The *Miller* reasoning was thus premised on the view that the administrative estimate was conclusive.

Congress plainly gave its acquiring authority, not the courts, the function of estimating just compensation for this purpose. And the lack of court review is evident from the fact that when the declaration is filed and the deposit made in court "title to the said lands * * * shall vest in the United States, and said lands shall be deemed to be condemned * * *." Had Congress intended court review of the declaration or the amount of the estimate, it would have provided for some court action by way of approval before title passed. It did not require any court action in this particular. Likewise, because it did not contemplate any court action, it made no provision for response by the condemnee or even for notice prior to vesting of title.

The tentative nature of the estimate was recognized in *United States* v. *1,997.66 Acres of Land, More or Less, Etc.*, 137 F.2d 8 (C.A. 8, 1943), where, in reversing the district court for refusing to permit increases and decreases in deposits made for various tracts, the court said (p. 14):

> The court could not govern its action by any personal opinion of whether the judgment of the

> acquiring officer or authority, as reflected in either the original or the revised estimate, was good or bad, *for that officer or authority had exclusive authority to estimate the amount of provisional just compensation*, and his good faith determination of the sum of money thus to be deposited was not subject to judicial review. * * * (Emphasis supplied.)

The delay necessarily resulting from court examination of the amount of the deposit in adversary proceedings demonstrates the lack of jurisdiction for the court to engage in such an undertaking. Court proceedings must be brought on by pleadings of some sort. Here the district court could not decide between whether this should be done by the answer or a separate motion to dismiss (R. 56, 64-65). Inevitably, delays occur in the legal procedures of filing motions, bringing them on for hearing and presenting the evidence and argument concerning the amount of compensation. Thus, in the instant case, while possession was sought on February 5, 1962, it was not until March 14, 1963, that the district court made its final ruling (R. 85, 87). In other cases the delay might, of course, be greater depending on how thoroughly the court might feel inclined to pursue the subject of value before ruling.

These time-consuming procedures prior to the award of possession are directly contrary to the purposes of the statute which, as the courts have emphasized, was enacted to prevent the government project from being delayed by legal proceedings, including appeals. *United States* v. *Miller*, 317 U.S.

369 (1943); *Catlin* v. *United States*, 324 U.S. 229 (1945). The taking of possession prior to payment has been exercised by the United States since the earliest days by physical seizure, leaving the landowner to his remedy of a suit under the Tucker Act. *United States* v. *Dow*, 357 U.S. 17, 21 (1958). In requiring the deposit of estimated compensation, Congress was conferring upon landowners benefits not constitutionally required. See *Garrow* v. *United States*, 131 F.2d 724 (C.A. 5, 1942), cert. den., 318 U.S. 765. This does not empower the court to enlarge that grant to include a power of the landowner or the court to control the amount of the deposit. It should be noted that the deposit in no way affects substantial rights of landowners. *Catlin* v. *United States*, 324 U.S. 229 (1945). The estimate in no way binds them, and has "no bearing whatsoever on value." *Chapman* v. *United States*, 169 F.2d 641, 644 (C.A. 10, 1948), cert. den., 335 U.S. 860.

We have already mentioned the delays that inevitably result from the exercise of the power asserted by the court below. Not to be ignored is the cumbersome procedure thereby created of, in effect, two trials as to the amount of compensation, the extent of the first trial depending upon the completeness of the court's review of the estimate.[4] The question here is purely one of statutory construction since the Decla-

[4] Here the basis of the alleged bad faith is the court's disagreement with the Government's theory of nominal compensation. There is every likelihood that, after the trial as to compensation, another appeal will be necessary if the court does not change its legal theory.

ration of Taking Act is creating rights not previously existing. To imply jurisdiction to review the administrative estimate of just compensation would be contrary to the terms of the statute and its purposes, would defeat its objectives and would impose completely unnecessary burdens on the court. Congress was satisfied that condemnees were sufficiently protected without such court review. It should not, we submit, be implied.

In re United States, 257 F.2d 844 (C.A. 5, 1958), cert. den., 358 U.S. 908, refused to imply such power. In that case, as in the present one, the district court was of the opinion that the estimate of just compensation must be a good faith, fair and honest estimate, and that if the court should be of the opinion that the estimate was not made in good faith, but arbitrarily, then the district court could vacate the declaration and refuse to give the Government possession. The Fifth Circuit rejected this view, saying (257 F.2d at p. 848):

> With deference to the contrary views of the district judge, we deem the settled law to be that the purported bad faith exception to the rule of finality of the administrative estimate of just compensation does not exist, that, in short, the courts have no jurisdiction to review the amount of estimated compensation, none to set aside or vacate a declaration of taking, none to refuse a declaration of possession on the grounds asserted here. If the law were otherwise, a district judge, under the guise of determining whether the declaration of taking was in good faith and the amount tendered sufficient to es-

> cape the charge that it was arbitrary or fraudulent, could superintend the whole act of taking, vesting title, and acquiring possession, and thereby prevent its accomplishment unless the amount estimated measured up to his idea of what that amount should be.

The district court, in the present case, acknowledged that it disagrees with the holding of the Fifth Circuit in *In re United States* (R. 66). It relies instead on the contrary views of the district court which the Fifth Circuit reversed as erroneous. *United States* v. *Certain Interests in Property (Hillsborough County)*, 161 F.Supp. 424 (S.D. Fla. 1958). Another case on which the district court relied for authority that a contention of bad faith is cognizable before the courts is *United States* v. *45.33 Acres (County of Princess Anne, Va.)*, 266 F. 2d 741 (C.A. 4, 1959) (R. 73).

A careful reading of the opinion shows that that case was based entirely on a failure to prosecute the action and that the complaint, as well as the declaration of taking, was dismissed. The court expressly refrained from deciding the good faith issue, saying, 266 F.2d at p. 744, " * * * we do not find it necessary to consider either the authority of the Court to inquire into the adequacy of the deposit or the good faith of appellant in making such deposit." This construction is supported by the Fourth Circuit's later opinion in *United States* v. *2,974.49 Acres (Clarendon County, S.C.)*, 308 F.2d 641 (1962), which reversed the dismissal of a declaration of taking.

The third case relied on by the district court to support its notion that it could inquire into the good faith of the acquiring agency is *United States* v. *44.00 Acres (Monroe County, N.Y.)*, 110 F.Supp. 168 (W.D. N.Y. 1953), rev'd, 234 F.2d 410 (C.A. 2, 1956) cert. den., 352 U.S. 916. Again, the district court's opinion was reversed by the court of appeals. The Second Circuit said in reversing, 234 F.2d at p. 415, " * * * the district court had no power to set aside the first amended Declaration of Taking, and its order so doing is void."

In summary, of the three cases relied on by the district court, two were reversed on the ground that there is no authority to vacate the declaration of taking, and the third was decided on other grounds expressly leaving the good faith issue open. Additional support for the Fifth Circuit's view is the similar holding as to nonreviewability of the selection of land to be taken. In *United States* v. *Mischke*, 285 F.2d 628, 631 (C.A. 8, 1961), the court held:

> We cannot accept the theory that the assertion by a defendant in a condemnation proceeding that the official, duly authorized by Congress to select the lands necessary to be taken for a public use, has acted in bad faith and arbitrarily and capriciously in making the selection, can transmute what has invariably been held to be a legislative question into a judicial one.[5]

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[5] We think that this case is clearly correct in holding that there is no "bad faith" exception from the rule precluding judicial review of administrative determinations to take particular property. Although there is dictum in lower

The two leading cases holding that it is beyond the power of the district court to vacate a declaration of taking are this Court's decisions in *United States* v. *Carey*, 143 F.2d 445, 450 (1944), and *United States* v. *Hayes*, 172 F. 2d 677, 679 (1949). These cases hold that, with the filing of a declaration of taking and deposit of estimated just compensation, title vests in the United States and the district court is thereafter powerless to dismiss the proceedings. The district court examined these and related cases only to conclude that "The cases appear to be in hopeless conflict as to whether a United States District Court has authority to vacate a declaration of taking, where a showing of lack of good faith is made" (R. 80). With regard to the *Hayes* and *Carey* cases, it is said that "The Court of Appeals for the Ninth Circuit has indicated that no such authority exists under ordinary circumstances, i.e., *where there is a failure to make a showing of bad faith* * * *" (*Ibid.*, emphasis supplied). Good faith or bad faith is not discussed in either the *Hayes* or *Carey* cases. The Ninth Circuit simply holds that, once title vests by the filing of the declaration of taking and the deposit of estimated just compensation, the court is powerless to vacate it. There is no intimation of any exceptions, for bad faith or otherwise.

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court decisions of existence of this power, the Supreme Court cases, properly analyzed, deny it. Compare *Berman* v. *Parker*, 348 U.S. 26 (1954), with the district court opinion, whose reasoning it rejected and whose judgment it modified by striking asserted limitations on the right of the agency to take property it thought it needed. *Schneider* v. *District of Columbia*, 117 F.Supp. 705 (D.C. 1953).

Nor do the other cases in which the district court purported to find a "hopeless conflict" contain a single instance in which the dismissal of a declaration of taking has been sustained. *Travis* v. *United States*, 287 F.2d 916 (C.Cls. 1961); *United States* v. *64.88 Acres (Allegheny County, Pa.)*, 244 F.2d 534 (C.A. 3, 1957); *United States* v. *284,392 sq. ft. (Kings County, N.Y.)*, 203 F.Supp. 70 (E.D. N.Y. 1962); *United States* v. *Certain Interests in Property (Cascade County, Montana)*, 163 F.Supp. 518 (D. Mont. 1958); *United States* v. *51.8 Acres (Nassau County, N.Y.)*, 147 F.Supp. 356 (E.D. N.Y. 1956); *United States* v. *48,752.77 Acres of Land, More or Less (Adams and Clay Counties, Neb.)*, 50 F.Supp. 563 (D. Neb. 1943). To the contrary, these cases generally support *Hayes* and *Carey* that a declaration of taking cannot be dismissed, title having vested in the United States. It is only by seizing upon individual expressions in these opinions, out of context, that any support at all can be found for the opposite conclusion. In addition, the district court might also have considered the recent Fourth Circuit decision in *United States* v. *2,974.49 Acres (Clarendon County, S.C.)*, 308 F.2d 641, 643 (1962), where the court, in following the *Hayes* case said, "Once it had determined that the condemnation was authorized by statute and that the statutory requirements had been complied with the court was without power to dismiss the condemnation proceedings and Declaration of Taking."

III

If The Order Dismissing The Declaration Of Taking Is Not An Appealable Order, It Is Requested That This Brief Be Treated As A Petition For Mandamus

A. *The order is appealable.*—The main issue in the case before the district court is the amount of just compensation, if any, to which the defendant is entitled. The taking of possession, deposit of estimated just compensation, and transfer of title under the Declaration of Taking Act are entirely ancilliary to, and separate from, the issue of just compensation.[6] Indeed, the declaration of taking procedure is so independent that the issue of just compensation could be determined without the procedure ever being used. *United States* v. *Dow*, 357 U.S. 17, 22 (1958). Therefore, when the district court set aside and vacated the declaration of taking in its order of March 14, 1963, that was a final and appealable order under the collateral orders doctrine.

In its enunciation of this doctrine in recent years the Supreme Court has said that those decisions are final and appealable under 28 U.S.C. sec. 1291 which "fall in that small class which finally determine claims of right separable from, and collateral to, rights asserted in the action, too important to be denied review and too independent of the cause itself to require that appellate consideration be deferred until the whole case is adjudicated." *Cohen* v. *Bene-*

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[6] Except only that the date of valuation and the amount of interest due are affected by the filing of the declaration of taking and deposit.

ficial Loan Corp., 337 U.S. 541, 546 (1949). This doctrine has been specifically applied, where as in the present case, "Appellate review of the order * * * at a later date would be an empty rite * * *." *Swift & Co.* v. *Compania Caribe*, 339 U.S. 684, 689 (1950).

At last year's term, the Supreme Court applied the collateral orders doctrine to two cases somewhat like our own. In our case, the district court has mistakenly exercised its jurisdiction to dismiss a declaration of taking. In so doing, the district court has exercised a jurisdiction it does not possess, as we have shown above, pp. 29-38.

In *Construction Laborers* v. *Curry*, 371 U.S. 542 (1963), the state courts of Georgia erroneously asserted their jurisdiction to deal with a controversy which was beyond their power and instead within the exclusive domain of the National Labor Relations Board. The Supreme Court held the Georgia court order determining jurisdiction was an appealable collateral order, saying, 371 U.S. at p. 548: "The issue on the merits, namely the legality of the union's picketing, is a matter entirely apart from the determination of whether the Georgia court or the National Labor Relations Board should conduct the trial of the issue." Similarly in *Mercantile National Bank* v. *Langdeau*, 371 U.S. 555 (1963), it was held that an order from a Texas state court determining which of two Texas courts had proper venue to entertain an action against two national banks was a final and appealable order. The Supreme Court said, 371 U.S. at p. 558: "This is a separate and independent matter, anterior to the merits and not enmeshed in the

factual and legal issues comprising the plaintiff's cause of action."

While it is believed that the order dismissing the declaration of taking is appealable, it is recognized that it is a close and difficult legal question not wholly free from doubt. The first case which must be disposed of in resolving this doubt is *Catlin* v. *United States*, 324 U.S. 229 (1945), where it was held that a "judgment" entered on a declaration of taking and a subsequent order denying the landowner's motion to vacate the judgment and dismiss the petition were not final and appealable orders. The basis of the decision is that the "judgment" entered on a declaration of taking is not a judgment at all in the true sense. The Court points out, at 324 U.S. p. 239, that "the statute does not purport in terms to authorize such a 'judgment' as was entered in this cause or to make its entry the event upon which title is changed, if so summary a procedure could be valid." This view, of course, supports the main burden of our argument in this brief that the district court has no jurisdiction to interfere with the filing of a declaration of taking. After clarifying the nature of the "judgment" in the case, one is left with the general rule that the order denying a motion to dismiss is never a final and appealable order, even when based on jurisdictional grounds. *Catlin* v. *United States*, 324 U.S. 229, 236 (1945); *Libby, McNeill & Libby* v. *Malmskold*, 115 F.2d 786, 787 (C.A. 9, 1940). And the *Catlin* case involved not, as here, a collateral issue but one of the two basic questions of all condemnation cases, i.e., the right to take.

In the present case, however, the fact is that the district court has dismissed the declaration of taking. This makes the present fact situation more analogous to the opposite rule that the order dismissing an action is a final, appealable order. *Aldridge* v. *States Marine Corp. of Delaware*, 265 F.2d 554, 555 (C.A. 9, 1959); *Allen* v. *Schnuckle*, 253 F.2d 195, 196 (C.A. 9, 1958); *Mantin* v. *Broadcast Music*, 244 F.2d 204, 205 (C.A. 9, 1957); *Fern* v. *United States*, 213 F.2d 674, 676 (C.A. 9, 1954); *Siegmund* v. *General Commodities Corp.*, 175 F.2d 952 (C.A. 9, 1949); *United States* v. *Hayes*, 172 F.2d 677, 679-680 (C.A. 9, 1949). Thus, it is believed that the *Catlin* case, which held that the order denying a motion to vacate the "judgment" on the declaration of taking was not appealable, would not be controlling here where the court dismissed the declaration of taking itself.

The second case which must be explained is *In re United States*, 257 F.2d 844, 846 (C.A. 5, 1958), cert. den., 358 U.S. 908, where it is said that: "As all, including the petitioner, agree, the order is not appealable." The statement that the petitioner, the United States, agreed that the order dismissing the declaration of taking is not appealable, undoubtedly arises from a misunderstanding of the Government's brief. There was no oral argument in that case. In its brief, the Government contended in the alternative, as it does here, that the writ of mandamus or prohibition should issue even if the order were not appealable. The brief takes the position that the order of dismissal is appealable, however.

The Fifth Circuit relies on two cases in addition to *Catlin* for the proposition that the order dismissing the declaration of taking is not appealable. *Dade County, Florida* v. *United States*, 142 F.2d 230 (C.A. 5, 1944), and *United States* v. *Richardson*, 204 F.2d 552 (C.A. 5, 1953). The *Dade County* case is very similar to the *Catlin* case in that the trial court simply entered an order on the validity of the declaration of taking and overruled the objections of the condemnee to the order. It is, for all practical purposes, the same as a denial of a motion to dismiss. In the *Richardson* case, the district court was exercising its undeniable prerogative to refuse to lend its judicial powers for the prosecution of a case where the plaintiff refused to answer requested admissions. That this was the view of the court of appeals is clear from the following, 204 F.2d at p. 555:

> The order of June 30, 1952, directs that this cause be not dismissed but that the cause and any prosecution of it by petitioner against Richardson and his lands should be abated. The order did not purport to interfere with the statutory consequences of compliance with the Declaration of Taking Act. It simply withdrew and suspended the judicial assistance which petitioner had invoked ex parte against appellee.

It is the Government's view in the present case that it is precisely because the district court's order does "purport to interfere with the statutory consequences of compliance with the Declaration of Taking Act" that the order is a final and appealable one.

B. *In any event, the district court's order dismissing the declaration of taking may properly be reviewed by this Court by writ of mandamus or prohibition.* — Assuming *arguendo* that the district court's order is not an appealable one at this time, *In re United States*, 257 F.2d 844 (C.A. 5, 1958), cert. den., 358 U.S. 908, is again directly in point that mandamus is proper. There can be little doubt that a later appeal would be futile. There will be no other final order in the case until after just compensation has been determined. The matter at issue is the Government's right of possession pending the determination of just compensation, that right deriving from the filing of the declaration of taking and deposit of estimated compensation. But once the actual compensation has been determined, the right of possession pending that determination is obviously a moot question. Since a later appeal would be frustrated, appeal is clearly an inadequate remedy and this Court may protect its appellate jurisdiction by use of a writ of mandamus. *LaBuy* v. *Howes Leather Co.*, 352 U.S. 249, 255 (1957); see *Bankers Life & Cas. Co.* v. *Holland*, 346 U.S. 379, 385 (1953); *Ex Parte Fahey*, 332 U.S. 258, 260 (1947).

An even stronger reason for the use of the writ of mandamus or prohibition than the inadequacy of the appeal is that the district court ruled on a matter beyond its jurisdiction: viz., the adequacy of the deposit of estimated just compensation. *In re United States*, 257 F.2d 844 (C.A. 5, 1958), cert. den., 358 U.S. 908. There is no question that this Court has supervisory power over the district courts of this

Circuit in aid of this Court's appellate jurisdiction. *LaBuy* v. *Howes Leather Co.*, 352 U.S. 249, 255, 259 (1957). The Supreme Court there said, in speaking of the right of the court of appeals to issue a writ of mandamus, "The question of naked power has long been settled by this Court." The historic use of writs of prohibition and mandamus directed by an appellate to an inferior court has been to afford an expeditious and effective means of confining the inferior court to a lawful exercise of its prescribed jurisdiction, or of compelling the inferior court to exercise its authority when it is its duty to do so. *Ex Parte Peru*, 318 U.S. 578, 583 (1943). Where the lower court has issued an order which is beyond its jurisdiction, the appellate court may issue a writ of mandamus to effect the vacation of such order. *United States* v. *Smith*, 331 U.S. 469 (1947). Where the district court has denied a litigant a constitutional or statutory right to a jury trial, the writ of mandamus is available to correct the wrong. *Beacon Theatres* v. *Westover*, 359 U.S. 500, 511 (1959). So here, where the district court had denied the Government its statutory right to possession, mandamus is available.

The power to mandamus extends to cases where its issuance is either an exercise of appellate jurisdiction or *in aid of appellate jurisdiction.* "That power protects the appellate jurisdiction which might be otherwise defeated and extends to support an ultimate power of review, though it not be immediately and directly involved." *United States* v. *District Court*, 334 U.S. 258, 263 (1948). Thus, the authority of this Court is not confined to the issuance of

writs in aid of a jurisdiction already acquired but extends to those cases which are within its appellate jurisdiction although no appeal has been perfected. *Roche* v. *Evaporated Milk Assn.*, 319 U.S. 21, 25 (1943).

CONCLUSION

The district court's memorandum and order of March 14, 1963, purporting to set aside and vacate the declaration of taking, should be declared null and void, and the district court instructed to enter an appropriate order granting possession of the property here involved to the United States.

Respectfully submitted,

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October, 1963.

Certificate of Examination of Rules

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

A. Donald Mileur,
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APPENDIX

In accordance with Rule 18, paragraph 2(f), the exhibits which are a part of the record in this case were identified, offered and received as evidence at the following places in the record:

	Identified, offered and received as evidence without objection:
Exhibit #1, Map showing location of mining claims	R. 94
Exhibit #2, Aerial mosaic showing Elliott Creek Road	R. 97
Exhibit #3, Mr. Suchy's report of January 23, 1961, entitled "Comments on the proposed interruptable easement for the Elliott Creek Road within the boundaries of the W. L. Cobb, et al., placer claims."	R. 104
Exhibit #4, Letter from the Secretary of Agriculture to the Attorney General dated October 4, 1961, setting forth certain statements concerning the one dollar deposit	R. 105

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No. 188 36

In the
United States Court of Appeals
For the Ninth Circuit

UNITED STATES OF AMERICA, APPELLANT
v.
WILLIAM LUCIAN COBB, et al, APPELLEES

Appeal From The United States District Court
For the Northern District of California

Brief of Appellees

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SUBJECT INDEX

TABLE OF CASES

TABLE OF CASES Continued

STATEMENT

The appellees accept the statment of facts as outlined by the appellants, except as hereinafter excepted to or supplemented.

The United States brought suit for condemnation and immediate possession of some 40.52 acres of land (R. 21) for road purposes over and across approximately 21 mining claims owned by the appellees.

There is nothing in the record to indicate that any issue will be made as to the validity of the mining claims or the right of possession therein by the appellees. The subjacent support, or toe, to support the roadway and the area covered thereby, is not described in the complaint. This additional area will be extensive as it is noted that the area is hilly and in a steeply sloped—steep-walled canyon. (EX. 3 R. 104).

A report was made by one Milvoy Suchy, a mining engineer who was an employe of the Department of Agriculture to the Secretary of Agriculture commenting upon the proposed easement sought by the government. This report is dated January 23, 1961. (R. 103). A patent application filed by the appellees had been previously pending since the year 1960 on three of the claims. (R. 123). It was the duty of Milvoy Suchy to make appropriate reports in regard to the patent

claims to the Bureau of Land Management and to assist in the issuance of patents, and he was particularly assigned to review these claims (R. 93, 124). The report of Mr. Suchy made on January 23, 1961, to the Secretary of Agriculture contained the following statement:

> "The claimants, E. T. Cobb, et al, have stated that they intend to apply for patent to the entire group of placer claims. At the present time a patent application is pending before the Sacramento Land Office for three claims; the Alta, Bright Gold, and Old Gold claims. These claimants have done most of their testing within the boundaries of these three claims and it is possible that one or all three of these may go to patent. ." (EX. 3).

For some unexplained reason, the report required by Mr. Suchy to the Bureau of Land Management to assist the appellees in securing their patent, was not supplied by him until the month of November, 1962, (R. 124) after the government had filed its condemnation proceeding.

Milvoy Suchy had never previously appraised a mineral deposit for condemnation. (R. 107). The report that Suchy filed with the Secretary of Agriculture, which allegedly was solely relied upon by the said Secretary, did not estimate or appraise the damages that would occur to the property values of the appellees in case the easement were obtained by the government. The only reference in the report to the

effect of the easement upon the mining claimants is the last sentence of the report, to-wit:

> "The writer believes that the **mining claimants rights under the general mining law,** are unaffected by the provisions of the proposed interruptable easement." (EX. 3) (Emphasis supplied)

Although the Court repeatedly endeavored to get Mr. Suchy to state whether he had made an estimate of the monetary loss that would be suffered by the appellees, the witness either evaded the answer or in effect admitted he had made no attempt to so estimate. (R. 112-117). Counsel for the government endeavored to clarify the matter, but no testimony was submitted in support of the statements by counsel. (R. 117-118). Mr. Suchy made no effort to ascertain from mining engineers or prospective purchasers of mining claims, whether or not the value of the claims would be reduced by the proposed easement, and expressed little or no knowledge of the results. (R. 119-122). The appellees would be confined to mining the premises in accordance with the dictates and in the manner required by the Forest Service. (R. 129A).

Counsel for the government conceded that the issue on the hearing "is whether or not he (Suchy) submitted an estimate as to the damages of this particular easement to the Secretary of Agriculture and the Secretary of Agriculture **had a right to rely there-**

on." (R.130) (Emphasis supplied) The appellees, in case the easement were granted, would be denied the right to re-mine the property or return for the removal of any of the black sands or other potentially valuable minerals that would not be removed in the first mining of the property, because under the terms of the easement when the road was replaced by the government after the first mining, the easement would become permanent and the road could not thereafter be destroyed or removed by the appellees. (R.132-133)

No consideration was given by Mr. Suchy to the probability of additional damages to the appellees resulting from the bringing in of additional rock and materials to be placed on the roads by the government or the construction of the by-pass roads, or in repairs. (R.134-135)

The witness stated that he was under the impression that the government was only trying to get the right to use the road which had already been built across these mining claims. (R.99) However, he finally admitted that other roads such as the Dutch Creek Road would be constructed under the terms of the easement. (R.110-11) The court observed that although the witness testified the road would be no detriment, that it was obvious that the appellees would be required to remove materials they would

not ordinarily have to remove. The ignoring of this fact affected the Court's opinion of his testimony. (R.112)

There is included in the photocopies of the transcript of record prepared by the appellants the motions filed by the appellees on May 28, 1962. (R.60-61) However, appellant has failed to include in the photocopies of the transcript of record the affidavit of Eldred T. Cobb which was attached to and by reference made a part of the motions. In order that the Court may have ready access to the omitted affidavit, we are setting it forth in the appendix to this brief commencing on page 32.

In the Court's memorandum and order which is being appealed, the Court made a specific finding as follows, to-wit:

> "Under such a set of circumstances, it cannot be said that the estimate by the Department of Agriculture that just compensation for the taking of the easement would be $1 was made in good faith, that is, with a reasonable basis for belief as to its accuracy." (R. 79).

In reaching that conclusion, the Court heard the entire testimony of Mr. Suchy, the only witness selected by the government, and made the following comment in respect to that witness' testimony:

> "I deem it only fair to state that I, as the trier of the facts here involved, was not impressed with

Mr. Suchy as a witness. To be perfectly candid, his testimony was so unsatisfactory to me, as to leave me with a fixed and abiding doubt concerning the opinion expressed by him." (R. 75).

SUMMARY OF ARGUMENT

I

Failure of the government to comply in good faith with the requirements of the declaration of taking statute renders the declaration of taking a nullity, therefore the same can be set aside by the District Court.

Courts of appeal generally have recognized that the District Court has jurisdiction to inquire into the question of whether or not the condemning agency has in good faith complied with the requirements of the declaration of taking statute. The purpose of the inquiry is not to determine whether the amount of the deposit is adequate, but to determine whether the amount was arrived at in good faith in accordance with the requirements of the statute.

If the District Court does not have jurisdiction to determine whether or not the declaration of taking statute has been complied with in good faith, then landowners are left at the mercy of possible capricious, arbitrary, bad faith action by government agencies.

II

Where the good faith of the condemning agency is challenged by the landowner and is supported by a prima facie showing of lack of good faith, a justiciable issue is presented to the District Court and it is the duty of the District Court to hold a hearing to determine the issue of whether or not the acquiring agency acted in good faith in making its estimate of just compensation in the amount deposited with the declaration of taking. Appellees made a prima facie showing of lack of good faith through the affidavit of Eldred T. Cobb, which is set forth in the appendix of this brief. It then became the duty of the appellant to present evidence to overcome this prima facie showing. The District Court found that the government failed to establish that the estimate of just compensation was made in good faith and on the basis of some reasonable appraisal.

The findings of the District Court are supported by substantial evidence and should not be reversed or set aside on appeal.

The declaration of taking statute requires that an estimate of just compensation must be made by the condemning authority and the amount deposited in court. "Estimate" means to set a value on or to appraise. "Just compensation" means the value of the

property taken at the time of the taking. The evidence presented by the appellant affirmatively shows that a mining engineer without previous appraisal experience was selected to examine the mining claims; that he did not appraise the value of the easement taken nor did he make any attempt to place a dollar amount on the damages resulting from the taking of the easement. The report submitted to the Secretary of Agriculture by the Department's Mining Engineer was wholly inadequate and insufficient to serve as the basis for an estimate of just compensation for the value of the easement taken. The general counsel for the Secretary of Agriculture should have so advised him. Hence the purported determination of just compensation made by the Secretary of Agriculture does not comply with the requirements of the declaration of taking statute and is a nullity.

"Bad faith" implies a breach of faith or a failure to perform a duly imposed duty. The Secretary of Agriculture failed to perform the duty imposed upon him by the declaration of taking statute in that he purported to make an estimate of just compensation without having any reasonable basis upon which to base his determination; therefore, his action amounted to bad faith.

The mining engineer who examined the claims for

the Secretary of Agriculture also made a mineral examination of the claims and filed a report with the Bureau of Land Management in connection with a patent application made by the appellees on three of the claims. The patent application was filed in 1960 long prior to the filing of the condemnation complaint. The mining engineer made a written report to the Department of Agriculture on January 23, 1961, yet he failed to file a report with the Bureau of Land Management until November, 1962, thereby preventing the appellees' application for a patent from being processed until after the condemnation complaint and declaration of taking were filed. This long delay in filing his report with the Bureau of Land Management is further evidence of lack of good faith.

The purpose of the hearing before the District Court was to determine whether or not the amount of $1 deposited with the declaration of taking was an estimate of just compensation arrived at in good faith by the Secretary of Agriculture. The hearing did not consider the question of whether or not the amount deposited was adequate.

III

Appellees concur with appellant that the order of the District Court dated March 14, 1963, is an appealable order for the reason that the order makes a

final determination of rights of the appellant adverse to the appellant.

However, if the Court of Appeals is of the opinion that the order of the District Court is not appealable, then appellees concur with appellant that the order of the District Court should be reviewed under the petition for mandamus.

It is of importance to both parties that the issue presented be determined on its merits thereby eliminating the possibility of a subsequent appeal after the issue of just compensation has been tried in the District Court.

ANSWER TO SPECIFICATION OF ERROR I

POINTS AND AUTHORITIES

I

A District Court has jurisdiction to vacate a declaration of taking where, contrary to the implied requirements of the statute, the estimate of the value of the condemned property is made by the government in bad faith.

City of Oakland v. United States, 124 F. 2d 959, 963 (C. A. 9, 1942)

Simmonds v. United States 199 F. 2d 305, 307 (C. A. 9, 1952)

United States v. 44.00 acres of land, etc., 110 F. Supp. 168 Rev'd 234 F. 2d 410, 415 (C. A. 2, 1956)

United States v. 29.4 acres of land, 131 F. Supp. 84, 87 (D. C. New Jersey, 1955)
Travis v. United States, 287 F. 2d 916, 919 (Ct. of Claims 1961)
United States v. 45.33 acres of land, 266 F. 2d 741 (C. A. 4 1959)
United States v. 64.88 acres of land, 244 F. 2d 534 (C. A. 3)
United States v. Meyer, 113 F. 2d 387, 392 (C. A. 7, 1940)
United States v. Threlkeld, 72 F. 2d 464, 465 (C. A. 10, 1934)

The appellant contends that whether or not there was bad faith, or whether or not there was a compliance with the statute, the Courts are absolutely powerless to intervene or reverse any action taken by an administrative authority. The lower Court disagreed with this contention.

It is the position of appellees that the failure of the appellant to comply in good faith with the requirements of the declaration of taking statute renders the declaration of taking a nullity and, therefore, the same can be set aside by the District Court.

In the City of Oakland v. United States, 124 F. 2d 959, a case from the Court of Appeals, Ninth Circuit, at page 963, it is stated:

> ". . . The answer of the District Court to these suggestions merits quotation: 'Assuming for purposes of argument that it is ultimately determined that the declaration of taking is affected with fraud or bad faith, it would follow that the declaration of taking will be a nullity, ineffective to vest title, and that the judgment thereon would also be a nullity . . ."

The Ninth Circuit also recognized the power of the District Court to inquire into the question of bad faith on the part of the condemning agency in Simmonds v. United States, 199 F. 2d 305, 307 where it is stated:

> ". . . Discretion as to the extent, amount or title of property to be taken by the United States has been conferred by legislation upon the Secretary of the Army; and in the absence of bad faith or abuse of that discretion his determination is final . . ."

The District Court for the Western District of New York in United States v. 44.00 acres of land, 110 F. Supp. 168, 171 stated:

> ". . . There can be no doubt that the court may not substitute its judgment for what is just compensation for the administrative determination of the acquiring authority. That however, does not mean that the court is without power to review an administrative determination involving the statutory requirement under the declaration of taking statute of a statement of estimated just compensation, where the good faith of the acquiring authority is unequivocally challenged and where the challenge is supported by a prima facie showing of lack of good faith and noncompliance with the statute."

The above decision was appealed and the Court of Appeals for the Second Circuit in United States v. 44.00 acres of land, 234 F. 2d, 410, 415 reversed the decision of the District Court in dismissing the declaration of taking for the reason that the government with its first declaration of taking deposited $300,000 and with its amended declaration of taking deposited an additional $200,000. However, the Court of Appeals stated:

> ". . . We may concede, arguendo, that a court has jurisdiction to vacate a Declaration of Taking where, contrary to the implied requirements of the statute, the estimate of the value of the condemned property is made by the Government in bad faith. But here the estimate was raised to an amount which the evidence shows to have been arrived at in good faith . . ."

The Second Circuit thereby recognized that the question of lack of good faith could be inquired into by the District Court.

Appellant relies heavily on the case of in re United States 257 F. 2d 844 (C. A. 5, 1958), cert. den, 358 U. S. 908. This decision of the Fifth Circuit can be distinguished on the basis of the facts involved. In in re United States, a deposit of $100,000 was made with the filing of the original declaration of taking and thereafter the deposit was increased to $400,500. Based on these facts the Fifth Circuit held the District Court

could not properly dismiss the declaration of taking. In the instant case, the deposit is only $1.

The Court of Claims in Travis v. United States, 287 F. 2d 916, 919, has cited in re United States as authority for the statement:

> "It has been held that judgment entered on a declaration of taking cannot be vacated and that the Court has no power to strike the declaration itself in the absence of bad faith."

Thus, it is to be seen that the Court of Claims, being fully cognizant of the holding of the Fifth Circuit, refused to adopt the extreme views which the appellant now presses on this Court and apparently adopts the position which was approved by the Ninth Circuit in City of Oakland v. United States, supra, and Simmonds v. United States, supra.

We have found only two cases in which the government paid into Court only the sum of $1 with its declaration of taking. One case is United States v. 45.33 acres of land, 266 Fed 2d 741 (C. A. 4, 1959). In that case the government paid $1 into Court with its declaration of taking. The landowner challenged the good faith of the government in arriving at the estimated value of $1 and put on evidence to establish a prima facie case of lack of good faith. The government was given an opportunity to put on evidence to establish its good faith in arriving at the sum $1, but failed

to do so, whereupon the District Court dismissed the declaration of taking. The government then appealed to the Fourth District and contended that the District Court did not have power to review the question of good faith on the part of the government. The Fourth Circuit declined to review the question of good faith but held that the District Court had a right to dismiss the declaration of taking because the government refused to comply with the Court's ruling that it must present evidence to overcome the landowner's prima facie case of lack of good faith on the part of the government. The Court of Appeals thereby recognized the propriety of the District Court holding a hearing on the issue of lack of good faith.

The other case in which $1 was deposited is United States v. certain interests in property, 163 F. Supp. 518, 520-21 (D. C. Mont. 1958). The defendant landowners objected that the sum of $1 was a mere nominal deposit and did not comply with the statute. Thereafter, the United States amended its declaration of taking and increased the estimated just compensation to the sum of $75,000, which amount was deposited with the Clerk of the Court. The District Court then held that the United States had a right to make such amendment and that since the amount deposited in Court was substantial, that it cured the defect complained of by the landowners. A reading of this case

establishes that the District Court would not have permitted the declaration of taking to stand if the government had not increased its deposit from a nominal sum of $1.

Appellant, in its brief, cites United States v. Carey, 143 F. 2d, 445, 450 (C. A. 9, 1945) and United States v. Hayes, 172 F. 2d 677, 679 (C. A. 9, 1949) in support of its contention that the District Court does not have jurisdiction to dismiss a declaration of taking. It is to be observed that in neither of these cases was the issue of lack of good faith or non-compliance with the condemnation statute by the government raised. Hence, these cases are not in point.

Unless this Court follows those cases which indicate that the District Court may review the question of lack of good faith on the part of the government in arriving at its estimate of just compensation, the landowner will be at the mercy of arbitrary, capricious action on the part of government officials.

The United States Supreme Court in United States v. Miller, 317 U.S. 369, 381, 63 S. Ct. 276, 283, 87 L. Ed. 336, has stated that the purpose of the statute providing for a declaration of taking and the deposit of estimated compensation is two-fold. One purpose being to give the government immediate possession and relieve it of the burden of interest. The other to give the de-

fendant landowner immediate cash compensation to the extent of the government estimate of the value of his property. If the appellant in this case is permitted to deposit only the nominal sum of $1 with the Court upon the filing of its declaration of taking, and, if the District Court does not have power to review the good faith of the appellant in arriving at the estimate of $1, then the landowners are without remedy and by the capricious, arbritrary, bad faith action of a public official may be deprived of their property without the benefit of partial compensation while awaiting trial of the condemnation case on the issue of just compensation. If the rule argued for by the appellant is recognized, it means that any agency of the government can acquire immediate possession of any parcel of property within the Ninth Circuit by the device of depositing $1 with its declaration of taking regardless of value of the property involved and regardless of the lack of good faith on the part of the government agency in making the estimate of $1 as compensation to be deposited with the Court. This could result in reducing many landowners to a condition of poverty while awaiting trial of their condemnation cases. The rule contended for by the appellant will effectively eliminate the requirement of statute that an estimate of just compensation must be made and deposited with the Court.

ANSWER TO SPECIFICATION OF ERROR II

POINTS AND AUTHORITIES

I

Where the good faith of the acquiring authority is unequivocally challenged and is supported by a prima facie showing of lack of good faith and non-compliance with the statute, a justiciable issue is presented.

Simmonds v. United States, 199 F. 2d 305, 307 (C. A. 9, 1952)
United States v. 44.00 acres of land, 110 F. Supp 168, 171, reversed 234 F. 2d 410 (C. A. 2, 1956)
United States v. 45.33 acres of land, 266 F. 2d 741 C. A. 4, 1959)
United States v. 1,997.66 acres of land, 137 F. 2d 8, 14 (C. A. 8, 1943)

II

Findings made by the trial court will not be reversed on appeal unless clearly erroneous and will be affirmed, if supported by any substantial evidence.

Gailbreath v. Homestead Fire Insurance Co., 185 F. 2d 361 (C. A. 9, 1950)
Smyth v. Barneson, 181 F. 2d 143, (C. A. 9, 1950)

III

"Estimate" means to set a value on, or to appraise.

United States v. Foster, 131 F. 2d 3, 7 (C. A. 8, 1942)

IV

"Just compensation" is the value of the property taken at the time of the taking.

United States v. Johns, 146 F. 2d 92, 93 (C. A. 9, 1944)
Oliver v. United States, 155 F. 2d 73, 75 (C. A. 8, 1946)

V

"Bad faith" is a term of variable significance, hence of broad application. It implies breach of faith, wilful failure to respond to plain, well understood, statutory obligations.

National Labor Relations Board v. Knoxville Publishing Co., 124 F. 2d 875, 883 (C. A. 6, 1942)
7 C.J.S. 1317, Bad Faith

VI

The deposit of $1 nominal damages in Court does not constitute the deposit of just compensation required by the statute.

Park Amusement Co. v. McCaughn, 14 F. 2d 553, 556 (D. C. Penn. 1925)

ARGUMENT

Appellees in their answer (R. 37) in their amended answer (R. 42) and in their motion to dismiss declaration of taking filed May 28, 1962 (R. 60) unequivocally challenged the good faith of appellant and alleged that the appellant failed to comply with the requirements of 40 USC 258 a-f. Appellees established a prima facie case of lack of good faith by the affidavit of Eldred T. Cobb which was attached to, and by reference made a part of the motions to strike the declaration of taking and which affidavit is set forth in the Appendix to this brief on page 32. (This affidavit was omitted from the photocopy of the transcript of the motions to strike plaintiff's declaration of taking and for that reason is included in the Appendix.)

Based upon the prima facie showing of bad faith as made by the affidavit of Eldred T. Cobb, the District Court directed that a hearing should be held on the issue of bad faith and granted the appellant the opportunity to produce evidence to overcome the prima facie case made by appellees. At the hearing, the District Court did not permit the appellees to present any testimony relative to value of the property that is being taken in the condemnation proceeding. The hearing was limited to the presentation of evidence by the appellant as to whether the deposit of $1 was

made in good faith and on the basis of some reasonable appraisal (R. 74).

On the basis of the cases cited under Points and Authorities I, supra and of the cases cited under the Answer to Specification of Error I, it is submitted that the District Court was presented with a justiciable issue and had jurisdiction to hear and determine that issue.

At the hearing, the appellant produced only one witness, Mr. Milvoy Suchy, a mining engineer who was an employe of the United States Forest Service, and who testified that he had "never appraised a mineral deposit for condemnation" (R. 107) and that he did not place a value upon the easement taken or the damages resulting to the mining claims from the taking of the easement (R. 113). The appellant introduced in evidence as Exhibit 3 a report prepared by Mr. Suchy, dated January 23, 1961, entitled "Comments on the Proposed Interruptable Easement for the Elliott Creek Road within the Boundaries of the W. L. Cobb, et al, Placer Claims" (R. 104). This report was the only information that was submitted to the Secretary of Agriculture and was the only information that was available to, and used by, him in making his determination that the sum of $1 constituted an estimate of just compensation for the easement taken.

The Suchy report does not contain an appraisal of the value of the easement taken, nor does it contain an estimate of just compensation, nor does it contain an appraisal or estimate of damages to the property rights of the appellees resulting from the taking of the easement. The only reference in his report to the effect of the easement upon the mining claimants is found in the last sentence of the report which reads: "The writer believes that the mining claimants' rights under the general mining law, are unaffected by the provisions of the proposed interruptable easement" (Ex. 3). This was also noted by the District Court in its memorandum (R. 74).

The declaration of taking statute provides that "Said declaration of taking shall contain * * * (5) a statement of the sum of money estimated by said acquiring authority to be just compensation for the land taken." 40 U.S.C. 258a (5). In United States v. Foster, 131 F. 2d 3, 7 (C. A. 8, 1942), it is stated:

> ". . . 'Estimate,' on the other hand, means: 'To set a value on or appraise.' 'To form an approximate judgment or opinion regarding the value.' 'Calculate approximately.' 'To form an opinion of.' New Century Dictionary . . ."

From an examination of the Suchy report (Ex. 3) and from the further facts revealed by the testimony of Mr. Suchy, it is apparent that no one on behalf of the government set a value on, or appraised, or made

an approximate judgment regarding the value of, the easement. Hence it follows that the estimate of $1 as set forth in the letter of the Secretary of Agriculture to the Attorney General (Ex. 4) and in the declaration of taking, was not arrived at in accordance with the requirements of the declaration of taking statute. The District Court made such a finding in the order appealed from. (R. 78-79).

It is the contention of appellees that the deposit of $1 with the declaration of taking which was not supported by an appraisal, or estimate, of the value of the easement taken, was nothing more than the payment of a nominal sum into Court and does not meet the requirement of the statute that the amount of the just compensation should be estimated and paid into Court. It follows, therefore, that such arbitrary action causes the declaration of taking to be a nullity.

Mr. Suchy, in his testimony, attempted to justify his failure to make an appraisal of the value of the easement taken by stating that it was his understanding that the appellees had been compensated for damages resulting from the construction of a road across their mining claims by the Bate Lumber Company by virtue of a $10,000 judgment granted the appellees against the Bate Lumber Company in a trespass action in the California State Court. (R. 107). In this connection the District Court found: (R. 78-79)

". . . His assessment that no damage would occur was based upon the supposition that whatever damage the road might cause had already been paid. In view of the fact that the easement herein would permit the Government to completely change the nature of the roads involved, this supposition seems patently erroneous. Mr. Suchy himself came close to admitting as much, in his statement that his report, based upon the above assumption, would be incorrect if such an assumption were incorrect.

"It thus appears that Mr. Suchy's determination that the easement herein would cause only nominal damage to the mining claims was based upon a clearly erroneous legal assumption as to the effect of the judgment against Bates Lumber Co. In view of said error, it follows that the report submitted by him to the Department of Agriculture was so defective as to amount to a mere guess as to the decrease in value to follow from the proposed easement herein. Under such a set of circumstances, it cannot be said that the estimate by the Department of Agriculture that just compensation for the taking of the easement would be $1 was made in good faith, that is, with a reasonable basis for belief as to its accuracy. It therefore follows that the Government's motion for an order of immediate possession must be denied."

It is a well established rule that the findings of the trial court will not be reversed unless clearly erroneous. Smyth v. Barneson, 181 F. 2d 143, 144 (C. A. 9, 1950).

The trial judge had the benefit of observing Mr. Suchy on the witness stand, his manner of answering questions, and was in a position to evaluate the weight

to be given his testimony. This caused the trial judge to state: "I deem it only fair to state that I, as the trier of the facts here involved, was not impressed with Mr. Suchy as a witness. To be perfectly candid, his testimony was so unsatisfactory to me as to leave me with fixed and abiding doubt concerning the opinion expressed by him." (R. 75).

Appellant, in its brief, argues that bad faith is present only where there is "fraudulent action" or where there is "actual malevolence, or spite directed toward the condemnee" (Ap. Br. 23). With this contention of appellant, we do not agree. In National Labor Relations Board v. Knoxville Pub. Co., 124 F. 2d 875, 883 (C. A. 6, 1942) it is stated:

> " 'Bad faith' is a term of variable significance, hence of broad application. In its simplest form, the phrase implies breach of faith, wilful failure to respond to plain, well-understood statutory or contractual obligations . . ."

See also 7 CJS 1317 where bad faith is defined as:

> "It has been said that 'bad faith' cannot be defined with mathematical precision, and is not a technical term used only in actions of deceit, but that it is a term of variable significance and rather broad application, and that its ultimate definition would depend upon the facts and circumstances of a given controversy . . ."

At page 1318 bad faith is defined as including "failure to perform a duly imposed duty" and the authority for

this definition is in re Hackett Hoff and Thiermann, 70 F. 2d 815, 817 (C. A. 7, 1934).

From the foregoing decisions, it is apparent that fraudulent action is not necessary to constitute action in bad faith.

The District Judge in the memorandum and order appealed from found that the Secretary of Agriculture had failed to act in good faith in making the determination that just compensation for easement taken was the sum of $1. His finding is amply supported by the evidence when it is considered that the Department of Agriculture sent a mining engineer without previous appraisal experience to make a survey of the mining claims involved and that the report submitted to the Secretary of Agriculture did not contain an appraisal of the mining claims nor an estimate of the value of the easement that was being taken by the government. Certainly, it was the duty of the general counsel for the Secretary of Agriculture to advise him that the Suchy report was wholly inadequate as a basis for making an estimate of just compensation. As the District Court pointed out in its colloquially with government counsel, if the Secretary of Agriculture had no obligation to secure competent advice and opinions upon which to base his estimate of just compensation, then it would be proper to have the Court's six-year

old grandson submit a report to the Secretary of Agriculture. (R. 130). Apparently, it is the position of appellant that a report from a six-year old child would be a sufficient basis for the Secretary of Agriculture's determination and that such action could not be reviewed by the courts.

Additional evidence to support the trial court's finding of bad faith is found in the conduct of Mr. Suchy who knew that a patent application had been filed by the appellees during 1960 prior to the filing of the condemnation action and that he had been assigned to investigate the claims as mineral examiner for the Bureau of Land Management. He testified that he had examined the claims and that at least one, if not three, of them were subject to patent. Apparently he had this knowledge when he submitted his report to the Secretary of Agriculture dated January 23, 1961. Yet, Mr. Suchy did not submit a report to the Bureau of Land Management until November, 1962. which was after the condemnation complaint and the declaration of taking in this case had been filed. If Mr. Suchy had been acting in good faith and in fulfillment of the duties of his office, he would have promptly submitted a report to the Bureau of Land Management so that the appellees' application for a patent could have been processed in a normal routine

manner long before the condemnation action was filed.

The District Court could not overlook the fact that the Suchy report and testimony failed to take into account that the appellees could be required to expend money to remove the Dutch Creek Road which has not yet been constructed. As stated in the memorandum and order of the District Court ". . . the government is presently acquiring the right to build a concrete road over what may now be merely a footpath . . ." (R. 77). The District Court further noted that if the mining operators desired to retrace their mining operation in the area in which the road had been rebuilt by the government, that the operators would face the additional task of removing rocks which had been used to buttress the rebuilt road. (R. 76). Yet, Mr. Suchy took the position that the mining claimants should be permitted only to mine their claims in one operation and that they should not be permitted to remine in any area. He refused to recognize that there is the possibility of technological development in the field of metals in the future. These were of importance to the Court because no appraisals could have been made of the value of the easement without giving consideration to these various factors of expense which were obvious. These deficiencies in the government's procedures in arriving at the determination of $1 disclose that the

action of the government was arbitrary and capricious and amounted to bad faith.

We submit that the conclusion of the trial court that the offer of $1 was an insult to the appellees is a reasonable conclusion based upon the fact that more than 40 acres of land is included within the easement and the other factors hereinabove set forth.

It must be remembered that the purpose of the hearing in the Disrict Court was not to determine the amount of just compensation that the appellees are entitled to receive for the taking of the easement across their mining claims. The only purpose of the hearing was to determine whether or not the amount of just compensation arrived at by the Secretary of Agriculture was an estimate made in good faith. The District Court expressly declared that this was the limit of his inquiry and declined to permit the appellees to put on any testimony relative to value.

Appellant on pages 31 and 32 of its brief, cites and quotes from United States v. 1,997.66 acres of land, 137 F. 2d 8, 14 (C. A. 8, 1943) to the effect that the amount of money determined by the condemning authority to be just compensation cannot be reviewed by the courts. However, we direct the Court's attention to the following quotation which also appears on page 14 of that report:

> ". . . So, too, if it should appear that the acquiring officer or authority is not acting in good faith, it may be that the court can properly refuse to allow the revised estimate to be filed or given effect as an amendment to the declaration of taking."

Appellant on page 35 of its brief, cites United States v. 2,974.49 acres, 308 F. 2d 641 (C. A. 4, 1962). We submit this case is not in point for the reason that the court of appeals found that the statutory requirements had been complied with and therefore the declaration of taking could not be dismissed. In the instant case, the issue is whether or not the statutory procedure has been complied with in good faith.

ANSWER TO PETITION FOR MANDAMUS

Appellees concur with appellant's position that the order of the District Court dated March 14, 1963, is an appealable order. This, for the reason that the order makes a final determination of rights of the appellant adverse to the appellant.

However, if this Court is of the opinion that the order of the District Court is not appealable, then appellees concur with appellant that the order of the District Court should be reviewed under the petition for mandamus.

If this appeal is not determined on its merits, it may well be that an appeal would be taken by the

government at the conclusion of the trial of the issue of just compensation. This for the reason that the measure of damages will be different if the declaration of taking is filed before or after the granting of the patent on one of the mining claims.

We shall not repeat the arguments that are set forth in our answer to specification of error I and II, but hereby direct the Court's attention to those arguments to be considered by the Court under this heading in event the Court determines that the order is not appealable and that the order is to be reviewed under the petition for mandamus.

CONCLUSION

The District Court's Memorandum and order of March 14, 1963 is abundantly supported by the evidence and by the weight of authority and should be affirmed. To hold otherwise, will be to establish the rule in the Ninth Circuit that any landowner may be dispossessed of his real property, be it his home or otherwise, upon the filing of a complaint in condemnation, a declaration of taking, and a deposit of $1 with the Clerk of the Court.

Respectfully submitted,
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CERTIFICATE OF EXAMINATION OF RULES

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Orval N. Thompson
of Attorneys for Appellees
Albany, Oregon 97321

APPENDIX

(Title of District Court and Cause Omitted)

AFFIDAVIT IN SUPPORT OF MOTIONS TO DISMISS COMPLAINT AND TO DISMISS DECLARATION OF TAKING

STATE OF OREGON)
) ss.
County of Linn)

I, ELDRED T. COBB, being first duly sworn on oath, depose and say:

That I am one of the defendants in the above-named condemnation action; that I reside at 215 South Fulton Street, Albany, Linn County, Oregon; that I am more than 21 years of age and that I am a citizen of the United States of America;

That I am one of the owners of the mining claims described in plaintiff's complaint and plaintiff's declaration of taking across which said mining claim plaintiff is seeking to condemn an easement for a road right of way; that I have had an interest in said mining claim since 1933 and that I have personally participated in the performance of assessment work and in mining operations that have been conducted upon certain of said claims during the intervening years; that I have personally checked the records of moneys that have been expended in connection with the assessment work performed upon and in connection with the development of said claims and that I personally know that in excess of $250,000 has been so expended and that during the past five years a sum in excess of $30,000 has been so expended, such sum is exclusive of attorneys' fees and expenses of litigation;

That I know of my own knowledge that said mining claims contain rich deposits of placer gold; that I personally have participated in conducting sampling and testing operations upon said claims and have

observed testing operations that have been conducted thereon by engineers and others; that evidence has been made available to the United States Department of Agriculture, Forest Service, based upon reliable authority of recognized mining engineers that there is no less than two million cubic yards of exposed gold-bearing and other mineral-bearing gravels upon said mining claims and that there is approximately five times more gold-bearing gravels which are covered by overburden; that a Mr. Milvoy Suchy, a mining engineer employed by the Forest Service of the United States Department of Agriculture, has by sworn deposition which was introduced in a trial in the Superior Court for Siskoyou County, California, and also in a demineralization hearing before the Bureau of Land Management of the United States Department of Interior, testified that, in his opinion, there is no less than 1,500,000 cubic yards of gold and mineral-bearing gravels exposed. These facts are and have for several years been available to the plaintiff and the agents and representatives of the plaintiff; that these gold-bearing gravels have been tested and the tests have disclosed that they contain gold values of approximately One Dollar ($1.00) per cubic yard; that the aforementioned Milvoy Suchy assisted in the tests that were made on one of these claims and that his reports of such tests are in the files of the Forest

Service of the United States Department of Agriculture and are available to plaintiff;

That during the years 1956 and 1957 a demineralization proceeding was filed against said mining claims by the Bureau of Land Management of the United States Department of Interior; that after the submission of the report of said Milvoy Suchy and the data secured by him as a result of tests made by him upon said mining claims that said demineralization proceeding was dismissed on the motion of the Government;

That prior to the filing of the above-captioned condemnation action the defendants who are the owners of said mining claims filed applications to patent three of said mining claims; that said patent applications have been diligently prosecuted and that the same are still pending; that I have been advised by the examiner for the Land Office before which said patent applications are pending that the Alta claim has been approved for a patent and that additional tests will be made upon the other two claims; namely, Bright Gold and Old Gold, which are covered by said patent applications; that patent applications are being prepared upon all of the other claims; that the filing of this condemnation action has operated to delay the filing of said patent applications on the other claims;

That said mining claims are situated in a deep ravine in the bottom of which flows Elliott Creek; that the banks of said ravine are very steep in most places; that the maintenance of a logging road over said mining claim at the location selected by plaintiff, or at any other location, will materially hinder the economic mining of said claims and will greatly reduce the value of said claims and will greatly reduce the amount of gold that can be removed therefrom; that because of the steepness of the canyon walls on both sides of Elliott Creek it is not possible to maintain a road at any location upon certain of said claims and conduct mining operations thereon at the same time and that an attempt to relocate the road at any other place on the claims in the areas where the canyon walls are steep will serve only to additionally interfere with mining operations; that the existence of any road at certain locations on certain of said mining claims will make mining of those claims virtually impossible and will make mining thereof uneconomic;

That my foregoing statements that it is not feasible to maintain any road upon certain of said mining claims and conduct mining operations thereon at the same time is substantiated by the opinion of Mr. G. Cleveland Taylor, a mining engineer of Sacramento, California, and of Mr. Hugh Wright, a mining engineer of Yreka, California; that the deposition of Mr. G.

Cleveland Taylor and the deposition of Mr. Hugh Wright was submitted to the Superior Court of the State of California in and for the County of Siskiyou in a case entitled "W. L. Cobb, et al, plaintiffs, v. Bate Lumber Company, et al, defendants, Case Number 16490," and that said depositions are and have been made available to plaintiff and various agents and representatives of plaintiff prior to the writing of this condemnation action;

That during the early part of the year 1956 Bate Lumber Company through its agents and contractors entered upon defendants' said mining claims without the permission or knowledge of the defendants and constructed a road across said mining claims over and along the area upon which plaintiff now seeks to condemn a right of way for a logging road; that these defendants protested the trespass of Bate Lumber Company upon their mining claims and filed a suit in the Superior Court of the State of California in and for Siskiyou County, Case Number 16490, seeking to restrain said Bate Lumber Company, its agents and contractors, from trespassing upon said mining claims; that the said Superior Court entered a Decree in said suit decreeing that these defendants are the owners of said mining claims and are entitled to the exclusive possession thereof and granting these defendants a permanent injunction against said Bate Lumber Com-

pany, its agents, contractors, and employees, from entering upon or otherwise trespassing upon said mining claims, or using said road so constructed by said Bate Lumber Company; that said Decree was entered in January, 1960; that during the 4-year period that the aforementioned case was in the Superior Court for Siskiyou County, California, these defendants were prevented from conducting operations upon said mining claims and as a result of attempts to conduct mining operations upon said mining claims these defendants learned that it would be impossible to conduct mining operations upon said mining claims and to maintain a logging road across said mining claims at the same time;

That agents and representatives of the Forest Service in the United States Department of Agriculture were fully informed of all phases of the above-entitled injunction suit between these defendants and Bate Lumber Company and were well aware of the Decree that was entered in said injunction suit in favor of these defendants; that during the four years consumed by the above-mentioned litigation a large number of log trucks hauled a large quantity of logs over the road constructed by said Bate Lumber Company across said mining claims; that the presence of said logging trucks and the heavy traffic thereof and the

frequency of their travels greatly impeded and interfered with defendants' attempted mining operations on their said mining claims; that if said road right of way is acquired by the Government and is open to travel by logging trucks, the presence of said trucks will effectively prevent defendants from operating their said mining claims by the use of heavy mining equipment, the fluming of water, and the use of explosives;

That all of the foregoing facts are obvious to and well known to the representatives of the Forest Service of the United States Department of Agriculture;

That the maintenance and operation of a road suitable for use by loaded logging trucks across said mining claims will result in large quantities of blasted rock, boulders, fill material and other debris being cast upon said mining claims; that the presence of said material will greatly interfere with mining operations on said mining claims; that the existence of a public road across said mining claims will expose said mining claims and any mining operations conducted thereon to the danger of pilferage and malicious destruction by persons using said road and will thereby materially reduce the market value of said mining claims; that all of the foregoing cited facts are well known to representatives and agents of the Forest Service of the

United States Department of Agriculture and were made known to them prior to the filing of the above-captioned condemnation action;

That said mining claims have a reasonable market value in excess of One Million Dollars and that purchasers are available who are willing to pay that amount if there is no roadway across said mining claims; that the existence of a road right of way across said mining claims such as plaintiff seeks to acquire in this action will render said mining claims valueless for sale or lease or other exploitation purposes;

That there has never been an appraisal made of said mining claims by the Government nor an appraisal made of the damages that will be suffered by defendants as a result of said road right of way being acquired across said mining claims by plaintiff in this condemnation proceeding; that there has been no good-faith determination made by any official or representative of the Government of the amount of money that would constitute just compensaation for the road right of way that plaintiff seeks to acquire across said mining claims in this condemnation action; that the sum of One Dollar ($1.00) which has been deposited with the Declaration of Taking by the plaintiff is a sham and capricious act and does not represent any compensation whatsoever as is required by Section 258 A

of Title 40 USC; that in making said deposit in the sum of One Dollar ($1.00) with the Declaration of Taking the agents and representatives of plaintiff acted capriciously and arbitrarily and in bad faith and in utter and complete disregard of the rights of these defendants and of the requirements of the Statute; that no representative of the Government has ever negotiated in good faith or otherwise with these defendats or any of them seeking to acquire said right of way; that representatives of the Government did threaten these defendants that unless these defendants gave the road right of way to the Government without compensation whatsoever that the Government would acquire immediate possession thereof by depositing the sum of One Dollar ($1.00) in Court and that the Government would thereby acquire the right to use said right of way without payment of just compensation into the registry of the Court; that the foregoing threats were made to these defendants in the office of Supervisor of the Rogue River National Forest in Medford, Oregon; that said representatives of the Government acknowledged to these defendants that said mining claims have a substantial value but that the Government was anxious to secure immediate possession of the road right of way and did not have a sufficient appropriation to pay the extent of damage that would be sustained by these defendants as the

result of a road right of way being acquired across the mining claims; that said Government representatives further acknowledged that they were aware that these defendants had exhausted most of their financial resources in the previous litigation with Bate Lumber Company and were not in a position to engage in protracted condemnation litigation;

That I am willing and able to be present and testify before the Court and on behalf of the defendants will produce and have present in Court the engineers and other expert witnesses who can give direct testimony as to the value of the mining claims in the event the Court desires to have further testimony.

Eldred T. Cobb

Subscribed and sworn to before me this 24th day of May, 1962.

Dolores Haslem
Notary Public for Oregon

My Commission Expires:
April 19, 1963

No. 18836

In the United States Court of Appeals for the Ninth Circuit

UNITED STATES OF AMERICA, APPELLANT

v.

WILLIAM LUCIAN COBB, ET AL., APPELLEES

Appeal from the United States District Court for the Northern District of California

REPLY BRIEF FOR THE UNITED STATES APPELLANT

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REPLY BRIEF FOR THE UNITED STATES APPELLANT

I

THE DISTRICT COURT HAS NO JURISDICTION TO DISMISS A DECLARATION OF TAKING

Appellees cite nine cases at the opening of their brief for the proposition that a district court has jurisdiction to vacate a declaration of taking where "the estimate of the value of the condemned property is made by the government in bad faith" (Br. 10-11). In only one of the nine cases cited did a district court

purport to vacate a declaration of taking because an estimate of just compensation had, in its opinion, been made in "bad faith." *United States* v. *44.00 Acres in Monroe County, New York*, 110 F. Supp. 168 (W.D. N.Y. 1953). This order was held to be null and void in *United States* v. *44.00 Acres in Monroe County, N.Y. (Odenbach)*, 234 F.2d 410 (C.A. 2, 1956), cert. den., 352 U.S. 916. In reversing, the Second Circuit said, "However, the district court had no power to set aside the first amended Declaration of Taking, and its order so doing is void." 234 F.2d at p. 415. It is only then that the court proceeds with the language quoted at page 13 of appellees' brief that "We may concede arguendo" that a declaration of taking may be set aside if not made in good faith.[1] Only one other of the nine cases cited involves the vacation of a declaration of taking for any reason. *United States* v. *45.33 Acres in Princess Anne County, Va.*, 266 F.2d 741 (C.A. 4, 1959). As has already been pointed out in our opening brief (p. 35), the vacation of the declaration of taking in that case was based on failure to properly prosecute the action, the issue of alleged judicial power to review claimed lack of "good faith" being again expressly left open.

The other seven cases presumably are cited because somewhere in the opinion, usually when referring to the broad discretion of administrative officers in selecting the property to be taken in condemnation

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[1] The very expression "concede arguendo" shows that, far from holding as appellees claim, the Second Circuit had doubt as to the existence of this alleged judicial power over the executive.

suits, "good faith" or "bad faith" are generally mentioned.[2] But no declaration of taking is vacated in any of them. None of these seven cases involves an issue as to the "good faith" or "bad faith" of the appropriate government officer in determining the estimated just compensation to be filed with a declaration of taking. Leaving aside the *Odenbach* case which was reversed by the Second Circuit, the only case of the nine cited which has any relevance to our specific problem is another district court opinion, *United States* v. *29.40 Acres of Land*, 131 F.Supp. 84, 88 (D. N.J. 1955), where it is said, "* * * this Court cannot weigh in this regard the evidence as to what amount the estimated just compensation should be, but only the question as to whether or not the amount deposited had, in fact, been 'estimated,' and not deposited as a mere nominal or arbitrary sum." The Government must, for the reasons set out in its opening brief, disagree with that court's conclusion that it is appropriate to have a preliminary hearing on estimated compensation, and rely instead on the

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[2] Appellees may want to add to their collection the recent case of *United States* v. *Agee*, 322 F.2d 139 (C.A. 6, 1963), where the court of appeals said, "We hold that the District Court was correct in reviewing the decision of the condemning authority to the extent of determining whether the decision [as to how much property to take] was made in bad faith * * *." 322 F.2d at p. 142. Here, again, however, the administrative determination of the property to be taken was upheld. And it will be noted that, after reviewing Supreme Court decisions holding administrative decisions unreviewable, the Sixth Circuit relied completely on dictum of one of its own earlier decisions for the proposition urged by appellees. Cf. footnote 5, p. 36, of our opening brief.

opposite conclusion reached in *In re United States*, 257 F.2d 844 (C.A. 5, 1958), cert. den., 358 U.S. 908. In any event, the *29.40 Acres* case supports our present appeal since it recognizes that the only question to be tried is whether an estimate was in fact made —regardless of the merits of that estimate—rather than the vague "good faith," or "bad faith" standard used by the district court in the present suit.

Appellees argue at page 14 of their brief that there is a split of authority between *In re United States*, *supra*, on the one hand and the Court of Claims decision in *Travis* v. *United States*, 287 F.2d 916 (1961), on the other. Appellees further contend that *Travis* is supported by this Circuit's decisions in *City of Oakland* v. *United States*, 124 F.2d 959 (1942), and *Simmonds* v. *United States*, 199 F.2d 305 (1952), in the theoretical split with *In re United States*. In fact, there is no split of authority. All four opinions are on different issues, and are entirely reconcilable. Only *In re United States* is directly in point on the issue of whether the district court has jurisdiction to decide whether the appropriate administrative official has estimated just compensation for a declaration of taking "in good faith." [3] The *Travis* case (on a collateral attack) holds that the declaration of taking in a condemnation suit is valid, and,

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[3] The purported distinction (Br. 13-14) of this case on the ground that there the deposit was not nominal does not tend to prove jurisdiction of the court to adjudicate an issue raised by an allegation that, whatever the amount, the deposit was made in bad faith. Jurisdiction cannot vary depending upon the amount of the deposit.

while noting the various grounds on which a declaration of taking might be attacked, no decision is made as to any of them. The *Travis* case does agree with the argument made by the Government in its opening brief that "under the facts in United States v. Carey, et al., 9 Cir., 1944, 143 F.2d 445, it was held that the dismissal of the condemnation petition would not result in a divesting of the title acquired by the United States as a result of a declaration of taking." 287 F.2d at p. 919. *Simmonds, supra,* holds that "Discretion as to the extent, amount or title of property to be taken by the United States has been conferred by legislation upon the Secretary of the Army; and in the absence of bad faith or abuse of that discretion his determination is final." 199 F.2d at p. 307. If a declaration of taking was involved in the case, it was not an issue on appeal. While a declaration of taking is part of the appeal in *City of Oakland, supra,* the attack is on the constitutionality of the procedure as a whole, and this Court upheld it. This Court did not have before it any issue of whether the district court has authority to hold a hearing on the "good faith" or "bad faith" of the administrative officer in estimating just compensation. We submit that *In re United States* is squarely in point here and should be followed.

II

THE ALLEGATION OF THE DEFENDANT IN A CONDEMNATION SUIT THAT THE ESTIMATE OF JUST COMPENSATION FOR A DECLARATION OF TAKING HAS BEEN MADE IN BAD FAITH DOES NOT PRESENT A JUSTICIABLE ISSUE

In answer to this point in our opening brief, appellees argue at some length on the facts of the case. The qualifications of Mr. Milvoy Suchy, and the details of how he arrived at his conclusion that appellees' mining claims[4] were not damaged by the taking of an easement over an existing roadway is examined. Mr. Suchy's report of January 23, 1961, is criticized because it does not say in the words which presumably appellees would have used that there was no damage to their mining claims.[5] (See appellees' brief,

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[4] We are not concerned at this stage of the proceeding as to the validity of appellees' mining claims. It may be assumed, *arguendo,* that their mining claims are good. However, we must point out that nothing said in this or the Government's Opening Brief is intended as an admission for purposes of this or any other litigation on the validity of these claims.

[5] There can be little doubt, after reading Mr. Suchy's report as a whole, that in his opinion the taking of the easement upon which there was an existing road would cause no further damage to the appellees' mining claims. The Suchy report is set out as an appendix to this brief for the convenience of the Court. Mr. Suchy approaches the matter primarily as a mining engineer who is knowledgeable of mining claims. He is not required to phrase his report in the terms which an expert witness might use when testifying in court on the issue of just compensation itself. To argue about his phrasing is simply to raise another irrelevant issue. Clearly,

p. 22). Mr. Suchy's testimony in the hearing below is criticized because he mentioned the trespass action against Bate Lumber Company in the state court. We have already pointed out in our opening brief (p. 22) that, fairly read, the record as a whole merely shows that Mr. Suchy took into account the condition the property was in on the date the condemnation suit was filed and did not blind himself to previous history. Appellees argue the weight to be given this evidence and the judicial standards on which it might be overturned. They argue (Br. 25) about what "bad faith" means, and conclude that it is a term of "variable significance" and "broad application" but attempt no definition as applied to this case. Hence, in appellees' view it can be said to mean whatever the district court wants it to mean on the individual facts of the case. Appellees argue that the legal officers at the Department of Agriculture failed in their duty to advise the Secretary. And they argue obscurely that Mr. Suchy's knowledge of a pending patent application in the Department of the Interior might have had some bearing on his "bad faith" or "good faith." [6] Finally, appellees (Br. 28) get into

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an administrative official, on the basis of this report by a qualified mining engineer, would be within the scope of his discretion in estimating the just compensation owing to be merely nominal.

[6] Appellees imply (Br. 27) that there was some unreasonable delay in the processing of their patent applications. There is nothing to show that such applications were not handled in the normal course and, in fact, one of them has been allowed.

issues about technological improvements in mining operations which may permit them to profitably remine the ground under the roadway at some unspecified future date as one basis for their claim of more than nominal compensation.

Appellees claim they may raise as a matter of right all these issues about the preliminary administrative estimate of just compensation which is ultimately binding on nobody. We have serious doubts about the relevancy of all these issues on the far more serious question of just compensation itself. Indeed, appellees' arguments point out most dramatically why the district court should not be allowed to delve into the myriad facets of a vaguely defined "good faith" or "bad faith" on a purely preliminary administrative estimate of the compensation. If the Government is wrong in its estimate, the landowners are made whole for the delayed payment of just compensation by the 6% interest which accrues on the deficiency. *Jacobs* v. *United States*, 290 U.S. 13, 17 (1933); *Seaboard Air Line Ry.* v. *United States*, 261 U.S. 299, 306 (1923). It is submitted that a hearing on the preliminary estimate of just compensation is not required by either the Constitution or the Declaration of Taking Act;[7] that no useful purpose is served by such a hearing; that it is harmful because it always raises a large number of tangential issues, results in a first adjudication of the issues normally determined at a jury trial on the merits, and only serves to delay both the Government's possession of the property and

[7] See Government's Opening Brief, pp. 12-16, for text.

the ultimate award of just compensation. Frustration of the purposes of the Declaration of Taking Act is clear.

CONCLUSION

The district court's memorandum and order of March 14, 1963, purporting to set aside and vacate the declaration of taking, should be declared null and void, and the district court instructed to enter an appropriate order granting possession of the property here involved to the United States.

Respectfully submitted,

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DECEMBER 1963

APPENDIX

(Suchy Report of January 23, 1961)

Plaintiff's Exhibit #3
(Identified and introduced at R. 104)

Rights-of-Way Acquired 5460
Elliott Creek Road No. 193
Eldred Cobb, et al.

Comments on the Proposed Interruptible Easement for the Elliott Creek Road Within the Boundaries of the W. L. Cobb, et al., Placer Claims

Reference is made to the maps included in the proposed condemnation case.

The road as shown on the map follows along the north slope of the Elliott Creek drainage. This slope has a thick talus cover for most of the distance within the boundaries of the claims. The road, as it is built today, required very little rock work, except near the west end of the group and at a few places where ridges interrupted the talus slopes. The Elliott Creek drainage, within the boundaries of the claims, is a steep-walled canyon with a fairly wide stream channel in the bottom. There are a few short distances within the claims where the canyon walls become almost vertical, and the channel becomes very narrow. These box-like canyons occur within the Daffodil No. 10 placer claim, Hazel placer claim, and along a distance of some 1,500 feet starting at the east end of the Pumpkin Seed No. 2 and continuing into the eastern portion of the Pumpkin Seed No. 1. The portion of the road through the box canyon areas was, for the most part, blasted out of the solid rock canyon walls, resulting in a road bed lying mostly on solid rock. The box canyon, being narrow, contains a very limited yardage of gravel;

however, some placering may be done by hand methods or with small power equipment that could cause the steep rock slopes of the road to slide away from the road bench. Mining in the narrow channels within the box canyon is rather improbable, and it is doubtful if an economic operation can be established.

The sampling results of various engineers, including Forest Service engineers that examined the property, indicate the auriferous gravels will have a value of somewhere between 30¢ to 75¢ per cubic yard. Estimates of the recoverable gravel present in the stream channel vary from 1½ million cubic yards to 5 million cubic yards. It is believed the recoverable gravel will run somewhere between 1½ million and 2½ million cubic yards. Test work done by the mining claimant shows that large boulders can be expected along the bedrock. Considering the previously-mentioned conditions, it is believed that the most practical and probably the only economic method for placering the Elliott Creek channel is by the use of either a floating washing plant or a dry-land washing plant which is fed by a dragline.

Mining operations with this kind of equipment would begin at the farthest point downstream where a continuous run of gravel occurs. This would probably mean that the bar beginning at the side line of the Hazel and Alta claims would be the site of the beginning of the operation. Since it is expensive to tear down and reassemble the washing plant, it is quite probable that the small bar below this point within the boundaries of the Pumpkin Seed No. 1 and Hazel claims would be worked by the use of portable sluice boxes rather than by the washing plant. The washing plant would be either a dry-land type on caterpillar tracks or a floating type on a boat hull. A dragline would then be set upstream of the wash-

ing plant, digging the gravel and swinging it into a hopper feeding either type of plant. This method of placer mining requires that the full width of the mineable channel is taken for economic reasons. Portions of the Elliott Creek Road would be breached as a result of this mining operation. This would occur only where gravel extended under the present road alignment, or where the side slopes would slough in to the excavation near the road. The portions of the road that might possibly be breached by the washing plant-dragline combination are as follows:

> Around 2,000 feet long along the road extending from about the middle of the Hazel claim to and including the Alta and Bright Gold claims.
>
> Beginning on the Daffodil No. 5 claim and extending upstream or to the east some 2,500 feet to about the center of the Daffodil No. 3 claim.

In addition, it is probable that three additional portions of the road may be breached as a result of placering narrow or isolated gravel bars by smaller equipment. These are: A distance of about 1,000 feet within the Pumpkin Seed No. 2, about 300 feet within the Pumpkin Seed No. 1, and about 1,200 feet within the Daffodil No. 10 and No. 9 claims. The damage that may be done to the road by the placering operation on the Pumpkin Seed No. 2 may be quite limited since most of this stretch of road has been blasted out of the steep side walls of the canyon. In regard to the other breaches, both by the washing plant and by a smaller scale placering operation, these will all fall within areas where the road has been built into the talus slopes of the drainage. The reconstruction of these portions should be relatively inexpensive and shoo-flies might be installed during mining operations that would permit hauling and access to continue without damage to either interest.

The possible breaching of some 7,000 feet of the road is, of course, conjectural. It is quite probable that there will be areas along the Elliott Creek channel that will not carry sufficient values to warrant placering and will be bypassed; also, as indicated by one of the claimants' tests, the edge of the channel may be too shallow and not carry sufficient values to warrant placering. Consequently, there may be much less encroachment upon the road alignment than is indicated. It is also possible that as placer mining progresses it will be found that it will be impossible to work the edges of the placer deposits where side cast material from the road slopes has diluted the auriferous gravels.

Another important factor to consider is the time element. A washing plant of the kind described, which is fed by a dragline, ordinarily could handle a half-million or more yards per year. Consequently, assuming 1½ million to 2½ million yards of available gravel, it is apparent that the mining operation, if pursued continually, could mine the entire gravel deposit in approximately three years. Considering the gravel may run between 30¢ and 75¢ per cubic yard and estimating that the placering method used will cost something like 35¢ per cubic yard, it is apparent that the profit margin does not allow for inefficient mining procedures. Consequently, the most economical operation would be continous whereby the equipment would be worked the maximum time avoiding costly shut-downs and waiting periods. Considering the present day costs of machinery and the resultant high amortization rate, together with the high wages for trained and common laborers, it is doubtful if the claimant can afford to expend his efforts in anything but the most efficient process of mining. It is always possible that the presence of shallow ground

and a large number of bedrock boulders together with possibly lower gold values than anticipated may result in a condition that will make mining the deposit at a profit impossible, and thus preclude any damage to the road whatsoever.

The claimants, E. T. Cobb, et al., have stated that they intend to apply for patent to the entire group of placer claims. At the present time a patent application is pending before the Sacramento Land Office for three claims; the Alta, Bright Gold, and Old Gold claims. The claimants have done most of their testing within the boundaries of these three claims and it is possible that one or all three of these may go to patent. In regard to the balance of the claims in the group, their chances of being patented are much less, and it is doubtful that many of these remaining will be patented.

It follows from the comments above that the interruptible type of easement would provide a reasonably continuous access across the Elliott Group of placer claims. There is a possibility that as much as 7,000 feet of road may be breached by mining operations; however, there is also reason to believe that mining operations may not cause near that amount of damage and maybe none at all. The cost of repairing breaches in the road alignment should be nominal as these probably would occur where the talus cover is quite deep, allowing the building of another road by side casting material.

The claimants are unrestricted in their mining of the Elliott Creek channel where there is no interference with the road alignment. The claimant must, according to the proposed interruptible easement, give the Government 60 days notice before they may conduct mining operations that will breach the road. This

is based on the results of a lawsuit by the claimants whereby they were compensated for the loss of the auriferous gravels that are not workable because of the road. Yet, under the provisions of the easement, the claimants may mine within the road alignment by merely giving 60 days notice. The writer believes that the mining claimants' rights under the general mining law are unaffected by the provisions in the proposed interruptible easement.

Date: 1-23-61

/s/ Milvoy M. Suchy
MILVOY M. SUCHY, Mining Engineer

APPROVED:

/s/ W. E. Bates
Acting Assistant Regional Forester

Date: 1-23-61

☆ U. S. GOVERNMENT PRINTING OFFICE: 1963 714998 508

No. 18838

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

LIMONEIRA COMPANY, a California corporation, ROGER DONLON, PAUL B. KERSTEN and E. B. ANTONELL, *et al.*,

Appellants,

vs.

W. WILLARD WIRTZ and ROBERT C. GOODWIN,

Appellees.

On Appeal From the United States District Court for the Southern District of California, Southern Division.

BRIEF FOR APPELLANTS.

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W. WILLARD WIRTZ and ROBERT C. GOODWIN,

Appellees.

BRIEF FOR APPELLANTS.

JURISDICTIONAL STATEMENT.

This is an appeal from a judgment entered June 10, 1963, by the United States District Court for the Southern District of California Southern Division, granting summary judgment to the defendants. The action was brought by the plaintiffs for themselves and on behalf of all users of Mexican National agricultural workers procured under the provisions of Public Law 78, as amended (65 Stat. 119; 7 U. S. C. A. 1461 *et seq.*) to enjoin the defendants from enforcing two so-called "adverse effect wage orders" made by the defendants under the provisions of Section 503, subsection (2) of said Act, and to obtain relief declaring that the said adverse effect wage orders were null and void and of no effect.

The jurisdiction of the District Court was based upon the provisions of 28 U. S. C. A. 1331 and 1332. Since the action arose under an Act of Congress regulating commerce, the court also had jurisdiction under the provisions of Section 1337. *Johnson v. Kirkland,* 290 F. 2d 440, 445, footnote 10; *Wickard v. Filburn,* 317 U. S. 111, 87 L. Ed. 122.

A timely Notice of Appeal from the order of the lower court, granting summary judgment to the defendants, was filed on July 10, 1963, by the plaintiffs. [R. 190.] Accordingly, the jurisdiction of this court is based on the provisions of 28 U. S. C. A. 1291.

STATEMENT OF THE CASE.

This is an action brought by the plaintiffs in the court below as employers of Mexican National agricultural workers procured under the provisions of Public Law 78 (65 Stat. 119; 7 U. S. C. A. 1461 *et seq.,* hereinafter referred to as "Public Law 78" or "the Act"), for themselves and on behalf of all other employers of Mexican National agricultural workers, to challenge the validity of certain "adverse effect wage orders" issued by the Secretary of Labor.

1. The Mexican Farm Labor Program.

The Agricultural Act of 1951, known as Public Law 78, was enacted by Congress to provide for the importation into the United States of Mexican National agricultural workers "for the purpose of assisting in such production of agricultural commodities and products as the Secretary of Agriculture deems necessary, by supplying agricultural workers from the Republic of Mexico . . .". (Sec. 501.)

The Act provided that the importation was to be "pursuant to arrangements between the United States and the Republic of Mexico . . .", and it empowered the Secretary, among other things, "to assist such workers and employers in negotiating contracts for agricultural employment . . .". (Sec. 501.)

Pursuant to the authority granted, the Migrant Labor Agreement of 1951 [R. 71] was negotiated with the Republic of Mexico and has since been amended from time to time by the two countries, and the Standard Work Contract [R. 94], also from time to time amended, was prescribed, setting forth the terms and conditions of employment of the agricultural workers, which were commonly referred to as "braceros". In practice the Migrant Labor Agreement and the Standard Work Contract constitute the administrative regulations under which the program is administered.

In order to protect the wages and working conditions of domestic agricultural workers from harm resulting from the importation of foreign labor, Congress provided in the Act that no workers would be available for employment under the Act unless the Secretary of Labor first determined and certified that (1) sufficient domestic workers able, willing and qualified were not available, (2) the employment of such workers would not adversely affect the wages and working conditions of domestic agricultural workers similarly employed, and (3) reasonable efforts had been made to attract domestic workers for such employment at wages, standard hours of work, and working conditions comparable to those offered to foreign workers. (Public Law 78, Sec. 503; 7 U. S. C. A. 1463.)

Article 9 of the Migrant Labor Agreement provided that "Mexican workers shall not be employed in the United States in any jobs for which domestic workers can be reasonably obtained, or by an employer who is not giving preference in employment to United States domestic workers . . ." It was also required that domestic workers, in addition to being given preference in hiring, had to be paid not less than the wages being offered to Mexican Nationals. Therefore, in order to be eligible to employ Mexican Nationals and to retain this eligibility, an employer had to give such preference in hiring to domestic workers and had to pay them not less than the wages offered to Mexican Nationals.

Prior to the 1961 amendment, Article 15 of the Migrant Labor Agreement provided that "The employer shall pay the Mexican worker not less than the prevailing wage rate paid to domestic workers for similar work at the time the work is performed and in the manner paid within the area of employment, or at the rate specified in the work contract, whichever is higher. The determination of the prevailing wage rate shall be made by the Secretary of Labor."

For the first twelve years of the program the Secretary of Labor administered the Act by conducting a survey to determine the prevailing wage in the area in which braceros were to be employed and by ordering that the braceros could not be employed at a wage less than that determined as the prevailing wage in the particular area.

In 1959, however, the Secretary of Labor in the State of Texas initiated the practice of fixing a minimum piece rate for cotton. This practice was challenged in the case of *Johnson v. Kirkland,* 290 F. 2d

440, 443, on the ground that the Secretary of Labor had no authority to fix wages in agriculture.

In 1961, without any authorization by Congress, Article 15 of the Migrant Labor Agreement and Article 4 of the Standard Work Contract were amended to provide that the employer should pay the Mexican worker the prevailing rate or at the rate "determined by the Secretary of Labor as being necessary to permit him to certify in accordance with the provisions of Article 9(a) of the Agreement, whichever is higher."

It was under and in accordance with this amendment to Article 15 of the Migrant Labor Agreement that the Secretary of Labor proceeded to issue the so-called "adverse effect wage orders".

2. The Facts of This Case.

On March 29, 1962, Arthur J. Goldberg, then Secretary of Labor, issued an order which determined that he could not certify that the employment of Mexican agricultural workers at rates lower than those specified in the order would not adversely affect the wages and working conditions of domestic agricultural workers similarly employed. [R. 11, 12.]

On October 19, 1962, Robert C. Goodwin, acting pursuant to authority delegated to him by the Secretary of Labor, issued an order which determined that he would be unable to certify that the employment of Mexican National agricultural workers at rates lower than those specified in the order would not adversely affect the wages and working conditions of domestic agricultural workers similarly employed. [R. 13, 14, 15.]

On December 20, 1962, the plaintiffs filed their action in the United States District Court for the Southern District of California, Southern Division, asking the court to enjoin the enforcement of said orders and to declare that said orders were null and void because they constituted the fixing of wages in agriculture and were beyond the scope of the authority of the Secretary of Labor under the provisions of Section 503(2) of Public Law 78 (7 U. S. C. A. 1463). [R. 2.] The said action was brought by the plaintiffs for themselves and on behalf of all users of Mexican National agricultural workers procured under the provisions of Public Law 78, and it alleged that the questions to be litigated involved common questions of law and fact affecting the rights of all such users in exactly the same manner as the plaintiffs were affected, and a common relief was sought. [R. 3.]

In their Second Cause of Action the plaintiffs alleged that if the provisions of Public Law 78, Section 503(2) (7 U. S. C. A. 1463) did in fact give the Secretary of Labor the authority to issue the so-called adverse effect wage orders, then said Section 503 (7 U. S. C. A. 1463) was invalid because it constituted a delegation of legislative authority to an administrative official and was consequently unconstitutional and void. [R. 8.]

On April 29, 1963, the defendants filed their Motion for Summary Judgment, which motion came on for hearing on May 20, 1963. In the defendants' Points and Authorities [R. 64] and in the court's opinion it was admitted that the defendants' action constituted the fixing of a minimum wage. [R. 186.] On June 10, 1963, the District Court gave judgment to the defend-

ants on their Motion for Summary Judgment, holding: "Inasmuch as it is found that there are no grounds for distinction, [Between findings of adverse effect based on prevailing wages rather than minimum wages] there can likewise be no claim of unconstitutionality." [R. 180.] The court held further: "The 'adverse affect' is what the statute is designed to prevent, and the fixing of a minimum wage rate would appear to be a much more effective means of preventing an 'adverse affect' than using the prevailing wage rate as a criteria." [R. 186.]

From this judgment this appeal is taken. [R. 190.]

Statutes, Migrant Labor Agreement and Standard Work Contract.

Public Law 78—82d Congress, as Amended
(7 U. S. C. A. 1461 *et seq.*)

AN ACT

To amend the Agricultural Act of 1949.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Agricultural Act of 1949 is amended by adding at the end thereof a new title to read as follows:

"TITLE V—AGRICULTURAL WORKERS

"Sec. 501. For the purpose of assisting in such production of agricultural commodities and products as the Secretary of Agriculture deems necessary, by supplying agricultural workers from the Republic of Mexico (pursuant to arrangements between the United States and the Republic of Mexico, or after every practicable effort has been made by the United States to negotiate and

reach agreement on such arrangements), the Secretary of Labor is authorized—

"(1) to recruit such workers (including any such workers who have resided in the United States for the preceding five years, or who are temporarily in the United States under legal entry);

"(2) to establish and operate reception centers at or near the places of actual entry of such workers into the continental United States for the purpose of receiving and housing such workers while arrangements are being made for their employment in, or departure from the continental United States;

"(3) to provide transportation for such workers from recruitment centers outside the continental United States to such reception centers and transportation from such reception centers to such recruitment centers after termination of employment;

"(4) to provide such workers with such subsistence, emergency medical care, and burial expenses (not exceeding $150 burial expenses in any one case) as may be or become necessary during transportation authorized by paragraph (3) and while such workers are at reception centers;

"(5) to assist such workers and employers in negotiating contracts for agricultural employment (such workers being free to accept or decline agricultural employment with any eligible employer and to choose the type of agricultural employment they desire, and eligible employers being free to offer agricultural employment to any workers of their choice not under contract to other employers);

"(6) to guarantee the performance by employers of provisions of such contracts relating to the payment of wages or the furnishing of transportation.

"Sec. 502. No workers shall be made available under this title to any employer unless such employer enters into an agreement with the United States—

"(1) to indemnify the United States against loss by reason of its guaranty of such employer's contracts;

"(2) to reimburse the United States for essential expenses incurred by it under this title, except salaries and expenses of personnel engaged in compliance activities, in amounts not to exceed $15 per worker; and

"(3) to pay the United States, in any case in which a worker is not returned to the reception center in accordance with the contract entered into under section 501(5), an amount determined by the Secretary of Labor to be equivalent to the normal cost to the employer of returning other workers from the place of employment to such reception center, less any portion thereof required to be paid by other employers.

"Provided, however, That if the employer can establish to the satisfaction of the Secretary of Labor that the employer has provided or paid to the worker the cost of return transportation and subsistence from the place of employment to the appropriate reception center, the Secretary under such regulations as he may prescribe may relieve the employer of his obligation to the United States under this subsection.

"Sec. 503. No workers recruited under this title shall be available for employment in any area unless the Secretary of Labor has determined and certified that (1) sufficient domestic workers who are able, willing, and qualified are not available at the time and place needed to perform the work for which such workers are to be employed, (2) the employment of such workers will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed, and (3) reasonable efforts have been made to attract domestic workers for such employment at wages, standard hours of work, and working conditions comparable to those offered to foreign workers.

"In carrying out the provisions of (1) and (2) of this section, provision shall be made for consultation with agricultural employers and workers for the purpose of obtaining facts relevant to the supply of domestic farm workers and the wages paid such workers engaged in similar employment. Information with respect to certifications under (1) and (2) shall be posted in the appropriate local public employment offices and such other public places as the Secretary may require.

"Sec. 504. No workers recruited under this title shall be made available to any employer or permitted to remain in the employ of any employer—

> "(1) for employment in other than temporary or seasonal occupations, except in specific cases when found by the Secretary of Labor necessary to avoid undue hardship; or
>
> "(2) for employment to operate or maintain power-driven self-propelled harvesting, planting, or cultivating machinery, except in specific cases when found by the Secretary of Labor necessary for a temporary period to avoid undue hardship.

"Sec. 505. Workers recruited under this title who are not citizens of the United States shall be admitted to the United States subject to the immigration laws (or if already in, for not less than the preceding five years or by virtue of legal entry, and otherwise eligible for admission to, the United States may, pursuant to arrangements between the United States and the Republic of Mexico, be permitted to remain therein) for such time and under such conditions as may be specified by the Attorney General but, notwithstanding any other provision of law or regulation, no penalty bond shall be required which imposes liability upon any person for the failure of any such worker to depart from the United States upon termination of employment: *Provided,* That no workers shall be made available under this title to, nor shall any workers made available under this title be permitted to remain in the employ of, any employer who has in his employ any Mexican alien when such employer knows or has reasonable grounds to believe or suspect or by reasonable inquiry could have ascertained that such Mexican alien is not lawfully within the United States.

"Sec. 506. (a) Section 210(a)(1) of the Social Security Act, as amended, is amended by adding at the end thereof a new subparagraph as follows:

> "'(C) Service performed by foreign agricultural workers under contracts entered into in accordance with title V of the Agricultural Act of 1949, as amended.'

"(b) Section 1426(b)(1) of the Internal Revenue Code, as amended, is amended by adding at the end thereof a new subparagraph as follows:

"'(C) Service performed by foreign agricultural workers under contracts entered into in accordance with title V of the Agricultural Act of 1949, as amended.'

"(c) Workers recruited under the provisions of this title shall not be subject to the head tax levied under Section 2 of the Immigration Act of 1917 (8 U. S. C. sec. 132).

"(d) Workers recruited under the provisions of this title shall not be subject to any Federal or State tax levied to provide illness or disability benefits for them.

"Sec. 507. For the purposes of this title, the Secretary of Labor is authorized—

"(1) to enter into agreements with Federal and State agencies; to utilize (pursuant to such agreements) the facilities and services of such agencies; and to allocate or transfer funds or otherwise to pay or reimburse such agencies for expenses in connection therewith;

"(2) to accept and utilize voluntary and uncompensated services; and

"(3) when necessary to supplement the domestic agricultural labor force, to cooperate with the Secretary of State in negotiating and carrying out agreements or arrangements relating to the employment in the United States, subject to the immigration laws, of agricultural workers from the Republic of Mexico.

"Sec. 508. For the purpose of this title—

"(1) The term 'agricultural employment' includes services or activities included within the provisions of section 3(f) of the Fair Labor Standards Act of 1938, as amended, or section 1426(h) of the Internal Revenue Code, as amended.

"(2) The term 'employer' shall include an association, or other group of employers, but only if (a) those of its members for whom workers are being obtained are bound, in the event of its default, to carry out the obligations undertaken by it pursuant to section 502, or (b) the Secretary determines that such individual liability is not necessary to assure performance of such obligations.

"Sec. 509. Nothing in this Act shall be construed as limiting the authority of the Attorney General, pursuant to the general immigration laws, to permit the importation of aliens of any nationality for agricultural employment as defined in section 508, or to permit any such alien who entered the United States legally to remain for the purpose of engaging in such agricultural employment under such conditions and for such time as he, the Attorney General, shall specify.

"Sec. 510. No workers will be made available under this title for employment after December 31, 1963."

Article 15
WAGES

The employer shall pay the Mexican worker not less than the prevailing wage rate paid to domestic workers for similar work at the time the work is performed and in the manner paid within the area of employment, or at the rate specified in the work contract, whichever is higher. The determination of the prevailing wage rate shall be made by the Secretary of Labor.

No authorization will be issued by the Secretary of Labor under Article 10 of this Agreement on the basis of a job order specifiying a wage rate which he finds has been adversely affected by the employment of illegal workers in the area.

In no case shall the Secretary of Labor make an authorization on the basis of any job order which specifies a wage rate found by the Secretary of Labor to be insufficient to cover the Mexican worker's normal living needs. In cases where the condition of a crop makes it impossible for a Mexican worker working with normal diligence and application to earn enough at the prevailing wage rate to cover his normal living needs, even though working full time, the Secretary of Labor shall conduct an investigation, and where requested by the Mexican Consul a joint investigation shall be conducted in accordance with Article 30 of this Agreement, to determine the proper steps necessary to remedy the situation. If no satisfactory adjustment in the wage rate can be agreed upon with the employer, the Secretary of Labor shall, if possible, arrange for a transfer of the workers to other agricultural employment. If

no such transfer can be effected within 5 days the Secretary of Labor shall terminate the work contract, and the employer shall, at his expense, return the worker to the reception center. Nothing in this paragraph is intended to affect the provisions of Article 25 of this Agreement.

The Mexican Consuls and the representatives of the Secretary of Labor shall exercise vigilance to insure that the wage rate paid to the Mexican worker is not less than the prevailing wage rate for similar work in the area of employment and that wages are paid to the Mexican workers in accordance with such rate or with any increase in such rate which may become effective in the area during the period of employment, but not below the minimum rate specified in the work contract. Increases in prevailing wage rates shall be put into effect immediately by the employer and shall not be contingent upon a formal request to do so by the Mexican worker, the Consul of Mexico, or the representative of the Secretary of Labor. Declines in prevailing wage rates shall be recognized and accepted by the Mexican worker, provided they do not fall below the rates specified in the work contract.

The Secretary of Labor shall periodically furnish the appropriate Mexican Consuls and Consuls General information with respect to the prevailing wage rates in their respective jurisdictions. The Secretary of Labor shall also furnish to the representative of the Mexican Government in Washington like information with respect to all areas in which Mexican workers are employed.

Any complaints concerning the failure to pay the prevailing wage rate shall be resolved by application of the procedure described in Article 30 of this Agreement.

The pay period for the Mexican worker shall be established at intervals no less frequent than those established for the employers' domestic workers; provided that, in no event shall the worker be paid less frequently than biweekly; provided further, that the employer may defer the payment of not to exceed a total of 4 days' earnings of such Mexican worker from one pay period to the next until the final payment of wages is made to him, at which time payment shall be made of all sums due to the Mexican worker.

Joint Interpretations and Amendments of March 1954

The wage rates paid to the Mexican worker may not be less than the prevailing wages for domestic laborers performing the same activity in the same area of employment as determined by the Secretary of Labor. The Secretary of Labor will give special attention, in conformity with Article 15 of the Agreement, to the fact that there shall not be issued authorizations which specify a wage rate which, in his opinion, has been adversly influenced by the presence of illegal workers in the area of employment. The prevailing wage rates shall be communicated to the Secretary of Foreign Relations as the Secretary of Labor determines them but not less than once a month.

In each of the migratory stations of Mexico and in each of the reception centers of the United States there shall be fixed, in prominent places, bulletins in which are specified the prevailing wage rates for each type of employment in each area of employment in which Mexican workers from the respective migratory stations and

reception centers will be employed in order that these wage rates may be known in advance by the Mexican workers who, in any event, may discuss them with the employers and accept or reject them.

If the Secretary of Foreign Relations believes that the determination of the Secretary of Labor, with respect to a specific wage rate for a specific area, is incorrect, he will inform the Secretary of Labor of his views in the matter, furnishing the Secretary of Labor the information upon which he bases his conclusion so that, in case the Secretary of Labor concurs in this conclusion, he may use the powers granted him by Article 15 of the Agreement to withhold authorizations which include such wage rates.

In case the Secretary of Labor, after reviewing the information furnished him by the Secretary of Foreign Relations, does not find that prior determination is inaccurate a joint investigation will be undertaken by the appropriate representatives of the two Governments, if requested by the Secretary of Foreign Relations, in order that the Secretary of Labor may determine whether it is appropriate to make a new determination of the prevailing wage rate. The contracting of workers will not be interrupted meanwhile but the Government of Mexico may inform the workers at the migratory stations that a joint investigation will be made with respect to the wage rates in question. If, as a result of the joint investigation the investigators cannot reach an agreement as to the information to be submitted to the Secretary of Labor, the Government of Mexico may request the Secretary of Labor to consider any information it desires to present concerning the prevailing wages.

Standard Work Contract, as Amended.

Article 4

PAYMENT OF WAGES

The employer shall pay the Mexican worker not less than the prevailing wage rate paid to domestic workers for similar work at the time the work is performed and in the manner paid within the area of employment, or at the rate specified in the work contract, whichever is higher. The determination of the prevailing wage rate shall be made by the Secretary of Labor.

Migrant Labor Agreement of 1951, as Amended in 1961.

Article 15

WAGES

(a) The employer shall pay the Mexican worker not less than the prevailing wage rate paid to domestic workers for similar work at the time the work is performed and in the manner paid within the area of employment, or at the rate specified in the individual work contract which shall be the rate determined by the Secretary of Labor as being necessary to permit him to certify in accordance with the provisions of Article 9(a) of the Agreement, whichever is higher. The determination of the prevailing wage rate will also be made by the Secretary of Labor. The employer and the Mexican worker shall be bound by the Secretary of Labor's determination of the wage rate required to be paid under this Article, and such determination shall be final and conclusive.

(b) In no case shall the Secretary of Labor issue an authorization to an employer on the basis of any job order which specifies a wage rate found by the

Secretary of Labor to be insufficient to cover the Mexican workers' normal living needs. In cases where the condition of a crop makes it impossible for a Mexican worker working with normal diligence and application to earn enough to cover his normal living needs at the rate being paid by the employer, even though working full time, the Secretary of Labor shall conduct an investigation, and where requested by the Mexican Consul, a joint investigation shall be conducted, to determine a course of action necessary to remedy the situation. If no satisfactory adjustment in the wage rate can be agreed upon with the employer, the Secretary of Labor shall proceed in accordance with the applicable provisions of Article 7 of this Agreement. Nothing in this paragraph is intended to affect the provisions of Article 25 of this Agreement.

(c) The Mexican Consuls and the representatives of the Secretary of Labor shall exercise vigilance to insure that the wage rate paid to the Mexican worker is not less than the wage rate required to be paid under (a) of this Article for similar work in the area of employment and that wages are paid to the Mexican workers in accordance with such rate or with any increase in such rate which may become effective in the area during the period of employment, but not below the minimum rate specified in the work contract. Increases in prevailing wage rates shall be put into effect immediately by the employer and shall not be contingent upon a formal request to do so by the Mexican worker, the Consul of Mexico, or the representative of the Secretary of Labor. Declines in prevailing wage rates shall be recognized and accepted by the Mexican worker, provided they do not fall below the rates specified in the work contract.

(d) The Secretary of Labor shall periodically furnish the appropriate Mexican Consuls and Consuls General information with respect to the prevailing wage rates in their respective jurisdictions. The Secretary of Labor shall also furnish to the representative of the Mexican Government in Washington, D.C., like information with respect to all areas in which Mexican workers are employed.

(e) Any complaints concerning the failure to pay the wage rate required to be paid under this Article shall be resolved by application of the procedures described in Article 30 of this Agreement.

(f) The pay period for the Mexican worker shall be established at intervals no less frequent than those established for the employer's domestic workers; provided that, in no event shall the worker be paid less frequently than bi-weekly; provided further, that the employer may defer the payment of not to exceed a total of 4 days' earnings of such Mexican worker from one pay period to the next until the final payment of wages is made to him, at which time payment shall be made of all sums due to the Mexican worker.

Explanatory note: The amendment contained in paragraph (a) of Article 15 is to confirm the Secretary of Labor's authority to require payment of a wage rate determined by him to be necessary to avoid adverse effect even though such wage rate were higher than the prevailing.

The finality provision set forth in the last sentence of section (a) works no substantive change in the Agreement but merely makes more explicit the already existing requirement of the Migrant Labor Agreement

that as a condition of participating in the program employers of Mexican workers agree to be finally bound by the Secretary of Labor's determination of the prevailing wage rate.

Reference to the employer's obligation to provide at his own expense, for the return of the Mexican worker to the reception center upon termination of the work contract has been deleted since this matter is covered by Article 17. No substantive change in this aspect of Article 15 has been effected and the employer's obligation remains unchanged.

Joint Interpretation of 1961

Wage rates paid to the Mexican worker may not be less than the prevailing wages for domestic workers performing the same activity in the same area of employment as determined by the Secretary of Labor or the wage rate determined by the Secretary of Labor as necessary to avoid adverse effect upon the wages and working conditions of domestic agriculture workers similarly employed. The prevailing wage rates and the wages determined by the Secretary of Labor to be necessary to avoid adverse effect shall be communicated to the Secretary of Foreign Relations as the determination of such wages is made but not less frequently than once a month.

In each of the migratory stations of Mexico and in each of the reception centers of the United States there shall be fixed, in prominent places, bulletins in which are specified the prevailing wage rates for each type of employment in each area of employment in which Mexican workers from the respective migratory stations and reception centers will be employed in order that these

wage rates may be known in advance by the Mexican workers who, in any event, may discuss them with the employers and accept or reject them.

If the Secretary of Foreign Relations believes that the determination of the Secretary of Labor with respect to a prevailing wage rate for a specific area is incorrect, he will inform the Secretary of Labor of his views in the matter. He will furnish the Secretary of Labor the information upon which he bases this conclusion in order that the Secretary of Labor may consider such information in reviewing the matter.

In case the Secretary of Labor, after reviewing the information furnished him by the Secretary of Foreign Relations, does not find that prior determination is inaccurate a joint investigation will be undertaken by the appropriate representatives of the two Governments, if requested by the Secretary of Foreign Relations, in order that the Secretary of Labor may determine whether it is appropriate to make a new determination of the prevailing wage rate. The contracting of workers will not be interrupted meanwhile but the Government of Mexico may inform the workers at the migratory stations that a joint investigation will be made with respect to the wage rates in question. If, as a result of the joint investigation the investigators cannot reach an agreement as to the information to be submitted to the Secretary of Labor, the Government of Mexico may request the Secretary of Labor to consider any information it desires to present concerning the prevailing wages.

Standard Work Contract, as Amended in 1961.

Article 4

PAYMENT OF WAGES

(a) The employer shall pay the Mexican worker not less than the prevailing wage rate paid to domestic workers for similar work at the time the work is performed and in the manner paid within the area of employment, or at the rate specified in the individual work contract which shall be the rate determined by the Secretary of Labor as being necessary to permit him to certify in accordance with the provisions of Article 9(a) of the Agreement, whichever is higher. The determination of the prevailing wage rate will also be made by the Secretary of Labor. The employer and the Mexican worker agree to be bound by the Secretary of Labor's determination of the wage rate, required to be paid under this Article, and such determination shall be final and conclusive.

SPECIFICATION OF ERRORS RELIED ON.

1. The District Court erred [R. 179] in concluding that the Secretary of Labor did not exceed his statutory authority in fixing a minimum wage to be paid Mexican National agricultural workers by Letter No. 1281 and by "Lettuce Harvest Determination", Exhibits A and B to Complaint. [R. 11, 12, 13, 14, 15.]

2. The District Court erred in concluding that there is no substance to the claim that Section 503 of the Act is unconstitutional. [R. 179.]

3. The District Court erred in concluding that there are no grounds for distinction between the Secretary of Labor's determination of adverse effect based on pre-

vailing wage and his determination based on a minimum wage. [R. 179.]

4. The District Court erred in failing to grant the injunctive and the declaratory relief prayed for by the appellants as against the aforementioned adverse effect wage orders. [R. 179, 188.]

5. The District Court erred in granting summary judgment to the appellees. [R. 179, 188.]

QUESTIONS PRESENTED.

1. Whether Section 503(2) of the Act (7 U. S. C. A. 1463) gives the Secretary of Labor the authority to fix minimum wages in agriculture as was done by the Secretary in the two so-called adverse effect wage orders.

2. In the alternative, and assuming that Section 503(2) (7 U. S. C. A. 1463) does give the Secretary of Labor the authority to fix a wage in agriculture, whether said Section 503(2) is invalid because it grants legislative authority to an administrative official.

SUMMARY OF ARGUMENT.

The two adverse effect wage orders purportedly issued under the authority of Section 503(2) of Public Law 78, 7 U. S. C. A. 1463 (hereinafter referred to as "the Act") by the Secretary of Labor are illegal because they constitute the fixing of a wage in agriculture, and consequently are in excess of the authority given the Secretary of Labor by the statute.

The authority of an administrative officer acting under an Act of Congress must be strictly limited by the terms of the Act. Section 503(2) authorizes the Sec-

retary of Labor only to determine and certify whether the contemplated employment of Mexican Nationals will adversely affect the wages and working conditions of domestic agricultural workers. Adverse effect must be measured against prevailing wage and can only result from the payment of less than the prevailing wage to Mexican Nationals. This interpretation of the statute urged by the appellants is supported by the following:

1. The language, which is clear and unambiguous, the common ordinary meaning of which is that the Secretary of Labor shall certify and determine whether adverse effect will occur. The plain and simple language does not mean that the Secretary of Labor shall fix a wage which will enable him to determine and certify that no adverse effect results.

2. Section 501(5) of the Act, which makes it clear that the wage to be paid Mexican Nationals is to be a negotiated wage and not a wage fixed by the Secretary of Labor.

3. The 1955 amendments to Section 503(2) which make it clear that Congress intended only that the Secretary of Labor make a survey to determine the prevailing wage and base his adverse effect wage determination thereon.

4. The Fair Labor Standards Act, which exempts agriculture from the provisions of the minimum wage laws; therefore Section 503(2) must be interpreted as being in harmony with this expressed intention of Congress to exempt agriculture. The interpretation insisted upon by the Secretary of Labor would constitute a repeal by implication of the agricultural exemption of the Fair Labor Standards Act.

5. The administrative interpretation of Section 503(2) as written into the Migrant Labor Agreement and the Standard Work Contract prior to the 1961 amendment, followed by the Department of Labor for the first twelve years of the Migrant Labor Program.

6. The entire legislative history of Public Law 78, Public Law 78 in general, and Section 503(2) in particular, which show clearly the intention of Congress that the authority of the Secretary of Labor was to be limited to the determination of adverse effect by reference to prevailing wage; it shows that Congress did not intend to authorize the Secretary of Labor to fix a wage in agriculture, and the legislative reports repeatedly warn the Secretary of Labor against this attempted encroachment on the prerogatives of Congress.

7. Finally, the fixing of a minimum wage is a legislative act. If Congress did in fact intend to give the Secretary of Labor the power to fix wages in agriculture, or in any other part of the economy, Congress thereby made a delegation of legislative power to an administrative official. Such a delegation of legislative power is illegal and unconstitutional because it was not accompanied by proper standards and limits. Congress must be presumed, however, not to have intended to make an invalid delegation of legislative authority, and where another interpretation is open to the court, the court is compelled to adopt such other interpretation. The interpretation offered by the appellants avoids invalidating the Act in question.

ARGUMENT.

I.

THE POWER EXERCISED BY AN ADMINISTRATIVE OFFICIAL UNDER AN ACT OF CONGRESS IS STRICTLY CIRCUMSCRIBED BY THE TERMS OF THE ACT.

A power conferred on an administrative official by the legislature is necessarily circumscribed and limited by the statute conferring or delegating that power. It is only the power to carry into effect the will of the legislature, expressed by the legislation. Under the guise of exercising the power conferred or delegated, an administrative official may not make rules or regulations, or negotiate executive agreements with a foreign power, which are inconsistent with or out of harmony with or which alter, add to, extend, enlarge, subvert, or impair the Act being administered. Hence, acting under the authority of Public Law 78, the Secretary of Labor may not negotiate an executive agreement with the Republic of Mexico which enlarges his powers or goes beyond the scope of the authority given to him by the Act.

It is the province and the duty of the courts to scrutinize the acts of administrative officials to determine whether they exceed the legislative grant of authority and whether they infringe upon the rights of individuals who are affected by the administrative authority exercised. Applying this well known and established principle of constitutional and administrative law, the Supreme Court in the case of *Stark v. Wickard,* 321 U. S. 288, 88 L. Ed. 733, held:

> "When Congress passes an Act empowering administrative agencies to carry on governmental ac-

> tivities, the power of those agencies is circumscribed by the authority granted. . . . The responsibility of determining the limits of statutory grants of authority in such instances is a judicial function entrusted to the courts by Congress by the statutes establishing courts and marking their jurisdiction. . . ."

In the case of *Waite v. Macy,* 246 U. S. 606, 62 L. Ed. 892, an administrative board was given the power to establish standards of "purity, quality and fitness of all kinds of imported tea", and acting under this power the board excluded tea imported by the plaintiffs because of the presence of substances which the court found were not in any way deleterious. In holding that the board exceeded its powers Justice Holmes stated:

> "The Secretary and the board must keep within the statute . . . which goes to their jurisdiction."
>
> * * * * *
>
> "No doubt it is true that this court cannot displace the judgment of the board in any matter within its jurisdiction, but it is equally true that the board cannot enlarge the powers given to it by statute and cover a usurpation by calling it a decision on purity, quality or fitness."

Paraphrasing Justice Holmes, it is submitted that the Secretary of Labor cannot enlarge the powers given him by Congress and establish minimum wages, and cover the usurpation by calling it "a wage necessary to prevent adverse effect".

A. An Administrative Official May Not Enlarge His Powers Through the Expediency of Issuing Administrative Regulations.

The corollary of the above stated principle that an administrative official must act within the scope of the authority granted by Congress is that such an administrative official may not enlarge his powers by the simple expedient of writing and issuing administrative regulations. In administering Public Law 78 the Secretary may not amend the Migrant Labor Agreement, which is the administrative regulation under which the Migrant Labor Program is administered, to give himself authority not granted in the law itself. As stated by the court in *Panama Refining Co. v. Ryan,* 293 U. S. 388, 428, 79 L. Ed. 447:

> ". . . From the beginning of the government the Congress has conferred upon executive officers the power to make regulations, . . . 'not for the government of their departments, but for administrating of the laws which did govern.' *U.S. v. Grimaud,* 220 U.S. 506, 55 L.Ed. 563, 31 Sup. Ct. 480. Such regulations become, indeed, binding rules of conduct, but they are valid only as subordinate rules and when found to be within the framework of the policy which the legislature has sufficiently defined."

II.

THE AUTHORITY OF THE SECRETARY OF LABOR MUST BE DETERMINED BY A CONSTRUCTION OF THE PERTINENT PROVISIONS OF THE STATUTE IN QUESTION, APPLYING THE RULES OF CONSTRUCTION.

It is the duty of the courts to construe statutes for the purpose of determining whether a particular act done or omitted falls within the intended inhibition or commandment of such statute. The primary rule in construing statutes is to determine the will of the legislature. The legislative intent is the heart, the soul, and the essence of the law, and its ascertainment is the objective of judicial construction. *United States v. Stone,* 274 U. S. 225, 71 L. Ed. 1013; *Ebert v. Poston,* 266 U. S. 548, 69 L. Ed. 435.

The application of the rules of construction is the method by which courts determine the legislative intent. *Hassett v. Welch,* 303 U. S. 303, 82 L. Ed. 858.

A. There Is No Ambiguity in the Language.

A cardinal principle of construction is that a statute is open to interpretation or construction only where there is an ambiguity or where it will bear two or more possible interpretations. It may be construed only where the language of the statute requires such construction, as where it is of doubtful or obscure meaning such that reasonable minds might be uncertain or in disagreement as to the meaning. Where the language is plain and unambiguous and conveys a clear and definite meaning there is no occasion for resorting to the rules of statutory interpretation, and the court has no authority to look for or impose a different meaning.

Boggs v. Fleming, 66 F. 2d 855; *United States v. Missouri,* 278 U. S. 269, 73 L. Ed. 322.

An ambiguity is defined as a doubtfulness or doubleness of meaning, an indistinctness or an uncertainty of expression. *Black's Law Dictionary,* 2d Edition. The courts may not find ambiguity in statutory language which laymen are able to comprehend. *Portland v. Hoss,* 81 A. L. R. 1136. The rules of interpretation are resorted to only for the purpose of resolving an ambiguity, not for the purpose of creating it. In the absence of an ambiguity courts should adhere to the commonly accepted meaning of language and should not import other than such commonly understood meaning to the terms employed in the enactment of a statute. *Railroad Commission v. Quincy Railroad,* 257 U. S. 563, 66 L. Ed. 371; *United States v. Shreveport,* 287 U. S. 77, 77 L. Ed. 175.

The critical language in issue is contained in Section 503:

> ". . . determined and certified that . . . (2) the employment of such workers will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed."

The key words of this section and those conveying the Congressional intent are the following: "determined", "certified", "adversely affect", "wages" and "similarly employed".

Webster's Dictionary defines "determine" as follows: "to decide . . . To come to a decision concerning, as the result of an investigation, reasoning, etc.; to settle . . . to resolve."

"Certify" is defined as follows: "To attest authoritatively; to verify . . ."

"Adverse" is defined as follows: "Acting against, or in a contrary direction; antagonistic; . . . In hostile opposition to one's interests; calamitous; afflictive; . . ."

The word "wages" needs no definition. The wages referred to are those paid to domestic agricultural workers during the period of the employment of the Mexican Nationals concerning whom the certification is made.

The words "similarly employed" require no definition. They simply mean "doing the same kind of work."

Giving to the language of Section 503(2) the ordinarily accepted meaning of the words used, it is submitted that the section means that no workers shall be available unless the Secretary of Labor makes a finding or a decision, and attests authoritatively as to that decision, that the employment of the Mexican Nationals in question will not have a harmful result on the wages and working conditions paid to domestic workers doing the same kind of work during the time the Mexican Nationals are employed.

The wage paid to domestic workers doing the same kind of work as the Mexican Nationals is the prevailing wage for that particular type of employment. If the prevailing wage is paid to the Mexican Nationals, then the employment of such Mexican Nationals cannot depress the prevailing wage and no harmful result can possibly occur. Hence adverse effect is measured against prevailing wage and can only occur when less than the prevailing wage is paid to the Mexican Nationals.

To say that the language of Section 503(2) means that the Secretary of Labor shall arbitrarily fix a wage having no relationship to the prevailing wage which will enable him to "determine and certify that the employment of Mexican workers would not adversely affect the wages and working conditions and employment opportunities of domestic agricultural workers" is to read something into the statute which is not there. It is a strained and tortured interpretation of otherwise plain, simple and ordinary language.

Reduced to the simplest terms, the issue is this: Does Section 503(2) provide that the Secretary of Labor shall determine whether adverse effect will result, or does it provide that the Secretary shall fix and enforce a wage which will enable him to determine that adverse effect will not result. It is submitted that the former interpretation is the only interpretation which can reasonably be given to the language in question. Had Congress intended that the power of the Secretary was to raise the domestic wage rate, establish a minimum wage, or to improve working conditions of domestic agricultural workers in the future, Congress would have used clear and specific language to confer this power. This is only too evident when the language of Section 503 is compared with the language of the *Minimum Wage Law,* 29 U. S. C. A. Sections 206 and 213:

"§206. Minimum wages; effective date

"(a) Every employer shall pay to each of his employees who is engaged in commerce or in the production of goods for commerce wages at the following rates —. . ."

"§213. Exemptions

"(a) The provisions of sections 206 and 207 of this title shall not apply with respect to . . . (6) any employee employed in agriculture. . . ."

B. Construction by Reference to Other Parts of the Statute Supports Appellants' Construction Regarding Limits of the Secretary of Labor's Authority.

In 1955 Congress amended Section 503 by adding a second paragraph which provides:

> "In carrying out the provisions of (1) and (2) of this section, provision shall be made for consultation with agricultural employers and workers for the purpose of obtaining facts relevant to the supply of domestic farm workers and the wages paid such workers engaged in similar employment. Information with respect to certifications under (1) and (2) shall be posted in the appropriate local public employment offices and such other public places as the Secretary may require."

From this it is evident that Congress intended to establish the administrative procedure to be followed and the facts to be found by the Secretary of Labor in his consultation with employers and employees. These are the facts relating to the present supply of domestic farm workers and the wages presently paid such workers engaged in similar employment. If these are the facts upon which the Secretary was to base his adverse effect determination, then it is clear and obvious that Congress intended that adverse effect was to be measured against prevailing wage and the Secretary of Labor's adverse effect determination was to be based thereon. This intention on the part of Congress is clearly expressed by the statement in *Senate*

Report 1045 dated July 20, 1955, U. S. Code, Congressional and Administrative News, Vol. 2, 84th Congress; 1st Session 1955, page 2848, and which, in addition to proposing the amendment to Section 503, provided for a two year extension to Public Law 78:

> "It is believed that this amendment specifying the information to be obtained and the persons from whom it is to be obtained will clarify procedures presently used and improve operations of the Act."

That adverse effect was to be measured as against the prevailing wage was also the conclusion of the court in *Johnson v. Kirkland,* 290 F. 2d 440, 445, which observed:

> "This argument gains some support from the 1955 amendments to Section 1463. . . . The Act as to elements (1) and (2) requires that the Secretary make an actual field survey and then post his findings. Inquiry on wages would have to relate to the currently prevailing domestic wage rate."

The same conclusion was reached by the court in *Dona Ana County Farm & Livestock Bureau v. Goldberg,* 200 F. Supp. 210 (1961):

> "As both parties appear to agree, the Secretary of Labor is not authorized directly to fix wages under the Agricultural Act, but is only empowered to determine the actual prevailing wages paid to domestic workers in the area of employment which must be paid to Mexican National farm workers performing the same activity in the same area of employment."

The language of Section 501, subsection (5) is a further indication of Congressional intent as to the extent of the Secretary of Labor's authority under Section 503 (7 U. S. C. A. 1463):

> ". . . the Secretary of Labor is authorized— . . . (5) to assist such workers and employers in negotiating contracts for agricultural employment (such workers being free to accept or decline agricultural employment with any eligible employer and to choose the type of agricultural employment they desire, and eligible employers being free to offer agricultural employment to any workers of their choice not under contract to other employers);"

This plain, simple and unambiguous language indicates the Congressional intention that the wage paid the Mexican National be a negotiated wage and not a wage fixed or determined by the Secretary of Labor, but subject to the limitation that it be not less than the prevailing wage. This is clearly borne out by the "Joint Interpretation and Amendment of March 1954" to Article 15, Wages, of the Migrant Labor Agreement, which provides in part as follows:

> "In each of the migratory stations of Mexico and in each of the reception centers of the United States there shall be fixed, in prominent places, bulletins in which are specified the prevailing wage rates for each type of employment in each area of employment in which Mexican workers from the respective migratory stations and reception centers will be employed in order that these wage rates may be known in advance by the Mexican workers who, in any event, may discuss them with the employers and accept or reject them."

This Joint interpretation makes it abundantly clear hat both the Government of Mexico and the Secre- ary of Labor regarded the wage to be paid the Mexican National as one to be arrived at by negotiation and ıot one fixed by the Secretary of Labor.

In conclusion, therefore, it is submitted that a con- struction of Section 503(2), along with Section 501(5), eads to the inevitable conclusion that the Congressional ntent was that the wage rate paid to Mexican Na- ionals was to be a negotiated wage and not a wage ixed by the Secretary of Labor. The fact that the Secretary of Labor adhered to this interpretation for he first twelve years of his administration of the pro- gram is strong and compelling evidence of the fact hat this is the proper interpretation of Congressional ntent.

C. Construction by Reference to Other Statutory Enactments Supports Appellants' Contention Regarding the Limits of the Secretary of Labor's Authority.

1. The Purpose of Construction Is to Harmonize the Statute With the Over-All Legislative Scheme.

One of the prime rules of construction is that the court should take into consideration the general policy of the legislature and the overall legislative scheme as t is reflected in other statutes.

In 1938 Congress enacted the Fair Labor Standards Act, 52 Stat. 1060, 29 U. S. C. A. 201 *et seq.* Sec- ion 206 of the Act provided a minimum wage. Sec- ion 213 of the same Act set forth exemptions to the minimum wage section. Subsection (6) of Section 213 ncludes within the exemption "any employee employed n agriculture".

It must be presumed to have been the intention of Congress that all of its enactments which are not repealed should be given effect. Accordingly, statutes should be so construed, if possible, so as to give full force an effect to each other statute. The court should not assume that one or the other of related statutes is meaningless and of no operational effect. Consistency and harmony is of prime importance, and where it is possible to do so it is the duty of the court to adopt that construction of a statute which harmonizes and reconciles it with other statutory enactments.

Zip Mfg. Co. v. Pep Mfg. Co., 44 F. 2d 184;
Heiden v. Cremin, 66 F. 2d 943;
Burton v. Denver, 107 A. L. R. 564;
Smith v. Board of Trustees, 198 Cal. 301;
Ariz. Eastern R.R. Co. v. Matthews, 7 A. L. R. 1149.

If Section 503 were construed as giving to the Secretary of Labor the authority to prescribe a minimum wage in agriculture, then such interpretation would place Section 503 in conflict with the Fair Labor Standards Act agricultural exemption. It would nullify the said agricultural exemption. On the other hand, if Section 503 is interpreted as giving the Secretary of Labor only the authority to measure adverse effect as against the prevailing wage, then such interpretation would be completely consistent with and in harmony with the agricultural exemption of the Fair Labor Standards Act. For this reason it is submitted that the latter interpretation should be adopted.

2. Repeals by Inference or Implication Are Not Favored by the Courts.

As a general rule, the legislature when it intends to repeal a statute may be expected to do so in express terms by the use of words which are the equivalent of an express repeal. In any case, an intent to repeal by implication must appear clearly and unequivocally.

The courts will not presume that the legislature intended to repeal by inference. Indeed, the presumption is always against the intention to repeal except where express terms are used or where effect cannot be reasonably given to both statutes.

Therefore, Section 503 may not be interpreted as giving the Secretary of Labor the authority to fix a wage in agriculture where the effect would be to repeal that portion of the Fair Labor Standards Act which exempted agriculture from the minimum wage laws. It cannot be reasonably expected that Congress would have intended to give the Secretary of Labor the authority to act in a field where Congress in its wisdom saw fit not to act itself.

Posadas v. National City Bank, 296 U. S. 497, 80 L. Ed. 351;

West India Oil Co. v. Domenech, 311 U. S. 20, 85 L. Ed. 16;

Zip Mfg. Co. v. Pep Mfg. Co., 44 F. 2d 184;

Corn Exch. Savings Bank v. Smith, 78 A. L. R. 800;

United States v. Borden Co., 308 U. S. 188, 84 L. Ed. 181.

D. Construction by Reference to Long Established Administrative Practice Supports Appellants' Contention Regarding the Limits of the Secretary of Labor's Authority.

Another important guide to the construction of the Act in question is the interpretation placed thereon by the Secretary of Labor during the first twelve years of his administration of the migrant labor program under Public Law 78. The construction of the Secretary of Labor was written into the Migrant Labor Agreement and the Joint Interpretation thereto, and the Standard Work Contract, which constitute the administrative regulations of the Act, all of which the Secretary played an important part in drafting. Prior to 1962 Article 15 of the Migrant Labor Agreement provided:

> "The employer shall pay the Mexican worker not less than the prevailing wage rate paid to domestic workers for similar work at the time the work is performed and in the manner paid within the area of employment, or at the rate specified in the work contract, whichever is higher. The determination of the prevailing wage rate shall be made by the Secretary of Labor."

Article 4 of the Standard Work Contract contained the same provision in identical language.

The "Joint Interpretation and Amendment of March 1954" provides in part as follows:

> "The wage rates paid to the Mexican worker may not be less than the prevailing wages for domestic laborers performing the same activity in the same area of employment as determined by the Secretary of Labor. The Secretary of Labor will

give special attention, in conformity with Article 15 of the Agreement, to the fact that there shall not be issued authorizations which specify a wage rate which, in his opinion, has been adversely influenced by the presence of illegal workers in the area of employment. The prevailing wage rates shall be communicated to the Secretary of Foreign Relations as the Secretary of Labor determines them but not less than once a month.

"In each of the migratory stations of Mexico and in each of the reception centers of the United States there shall be fixed, in prominent places, bulletins in which are specified the prevailing wage rates for each type of employment in each area of employment in which Mexican workers from the respective migratory stations and reception centers will be employed in order that these wage rates may be known in advance by the Mexican workers who, in any event, may discuss them with the employers and accept or reject them."

During the first twelve years of the program the Secretary of Labor administered the program according to these provisions which he himself helped to draft.

The practice of the Secretary of Labor during this period of time was to conduct a survey in a particular area in order to determine the prevailing wage, and following this survey issued orders to the effect that he could not determine and certify that adverse effect would not result unless Mexican Nationals were paid a wage not less than the prevailing wage so determined in the particular area. In short, adverse effect was measured as against the prevailing wage in a given area, and no adverse effect was deemed to exist unless

and until the employers of braceros paid less than that prevailing wage.

However, in 1961 both Article 15 of the Migrant Labor Agreement and Article 4 of the Standard Work Contract were amended to provide that the employer shall pay the Mexican worker not less than the prevailing rate or the rate specified in the work contract which "shall be the rate determined by the Secretary of Labor as being necessary to permit him to certify in accordance with the provisions of Article 9(a) of the agreement, whichever is higher." Congress had not changed Section 503 of the law with respect to the determinations to be made by the Secretary of Labor. But without Congressional authority the Secretary assumed, pursuant to his own change in the administrative regulations, the authority to fix a minimum wage in agriculture, which he euphemistically called "the wage determined by the Secretary of Labor as being necessary to avoid adverse effect."

Construction and interpretation by an administrative agency of the law under which it acts provides a practical guide as to the interpretation of the law and is an experienced and informed judgment to which the courts and the litigants may properly resort for guidance.

White v. Winchester, 315 U. S. 32, 86 L. Ed. 619;

N. Y. v. Frank, 314 U. S. 360, 86 L. Ed. 277, *Annotation,* 84 L. Ed. 28;

Bowen v. Johnson, 306 U. S. 19, 83 L. Ed. 455;

Mintz v. Baldwin, 289 U. S. 346, 77 L. Ed. 1245;

Fawcus v. United States, 282 U. S. 375, 75 L. Ed. 379;

Luckenbach v. United States, 280 U. S. 173, 74 L. Ed. 356.

The long standing practice of the Secretary of Labor in the administration of the statute effectively expressed his understanding of the Congressional intent. When after a long period of such practice a change in the interpretation of the law is made, without Congressional authority, which substantially enlarges the authority of the administrative official, it is submitted that such change should be regarded with great suspicion and it should be incumbent upon the administrative official to explain such change.

1. Re-Enactment of the Law by Congress Constituted the Adoption of the Administrative Regulations in Effect at the Time.

Public Law 78 as enacted in 1951 was for a period of two years, and since that date Congress has repeatedly re-enacted Public Law 78 at the end of each two year period. The administrative construction followed by the Secretary of Labor for the first twelve years of the Migrant Labor Program was repeatedly confirmed and approved by each subsequent re-enactment of the law from 1951 to the present date. Congress was in fact cognizant of the established administrative practice of determining adverse effect on the basis of prevailing wage, as was provided in the Migrant Labor Agreement and the Standard Work Contract prior to the 1961 amendments. Each time it extended the Act without any change in its provisions it impliedly adopted the construction applied by the administrative authority. Therefore, the Congressional

intent that adverse effect was to be measured against prevailing wage is clearly established by such repeated re-enactment of the law.

Hartley v. Commissioner, 295 U. S. 216, 79 L. Ed. 1399;

Cook v. United States, 288 U. S. 102, 77 L. Ed. 641;

Johnson v. Manhattan, 289 U. S. 479, 77 L. Ed. 1331;

Luckenbach v. United States, 280 U. S. 173, 74 L. Ed. 356.

E. Statutes Must Be Construed so as to Give Effect to the Same—Not so as to Nullify.

It is argued elsewhere in this brief that if Congress gave the Secretary of Labor the power to fix wages, such grant of power would be a delegation of legislative authority which would be invalid for the reason that proper and sufficient standards were not laid down by Congress to guide the Secretary in the exercise of said power. A delegation of legislative power without such standards is invalid.

Opp Cotton Mills v. Administrator, 312 U. S. 126, 85 L. Ed. 624;

Schecter v. United States, 295 U. S. 495, 79 L. Ed. 1570;

Star Kist v. United States, 169 F. Supp. 268.

To interpret the statute as being an invalid grant of legislative power would in effect nullify part of the statute. In the construction of the statute the courts must necessarily start with the assumption that the legislature intended to enact an effective law, and the legislature is not presumed to have done a useless act

in enacting a statute which is invalid. Therefore, the court should, if reasonably possible, interpret any statute so as to give it effect. The court should not interpret a statute so as to nullify it, destroy it, emasculate it, repeal it, or defeat it. Where there is an alternative construction or interpretation which will avoid this result, the court must apply such other interpretation. There is such other interpretation or construction, *i.e.,* the one placed on the statute by the Secretary of Labor when the statute was first enacted, which interpretation was followed for the first twelve years of the administration of the Migrant Labor program. Such interpretation confines the Secretary to a determination of the adverse effect measured against prevailing wage. It avoids rendering the statute null and void and unconstitutional.

N. L. R. B. v. Jones & Laughlin, 301 U. S. 1, 81 L. Ed. 893;

Federal Trade Com. v. American Tobacco, 264 U. S. 298, 68 L. Ed. 696.

F. The Legislative History of the Act Proves That Congress Did Not Intend to Give the Secretary of Labor the Power to Fix Wages.

Basic to the interpretation of any statute is the ascertainment of the legislative intent. *United States v. Rosenbloom,* 315 U. S. 50, 86 L. Ed. 671; 50 Am. Jur. 200. This is best obtained by reference to the proceedings and debates of Congress and the Committee Reports on Public Law 78 and the periodic re-enactment thereof.

One indication of Congressional intent that adverse effect was to be measured by reference to the prevail-

ing wage is *Senate Report 1045* dated July 20, 1955, U. S. Code, *Congressional and Administrative News,* 84th Congress, 1st Session 1955, page 2844 at 2848, on the bill to extend Public Law 78 and amend Section 503. In explaining the reasons for the proposed amendment, which was enacted into law, the Report stated:

> "To assure that such conditions do not prevail, the committee has included an amendment to section 503. The amendment specifies that the Secretary is to obtain information on the availability of domestic workers and the wage rates paid to them from agricultural employers and farmworkers employed in the area where a shortage of domestic workers is reported to exist. . . . After the Secretary has made his determination pursuant to section 503, he shall cause to be posted in appropriate public places the number of workers to be imported, and such other relevant information respecting his certifications as he deems necessary. It is believed that this amendment specifying the information to be obtained and the persons from whom it is to be obtained will clarify procedures presently used and improve operations under the act."

Obviously, if the information to be obtained by the Secretary of Labor was the prevailing wage, then adverse effect was to be determined by the Secretary on the basis of the prevailing wage; otherwise the 1955 amendment would have served no purpose and would have prescribed useless action by the Secretary of Labor.

Also informative on the matter of Congressional intent is *Senate Report 2189* dated August 5, 1958, U. S.

Code, *Congressional and Administrative News,* 85th Congress, 2d Session 1958, page 3971 at 3973:

"The program requires many safeguards for the Mexican farmworkers who come into this country. They are guaranteed by our Government that their employers will comply with the provisions of their work contracts with respect to wages and transportation. Section 10 of their work contract guarantees to them the opportunity for employment for at least three-fourths of the workdays during their contract period. Furthermore, they are to receive the prevailing wage for similar work in the area where they are employed.

"The determination of the prevailing wage to be paid has been the subject of discussion at the public hearings. The committee is of the opinion that the duty of the Secretary of Labor in making such findings is quite simple. He should find the prevailing wage rate or rates actually paid to domestic workers in the area of employment and there is no necessity for alterations or use of formulas in the determination of such rates. If the prevailing rates so found are paid to Mexican farmworkers for the same work in the same area under the same conditions, the committee would consider prevailing wage requirements to have been met."

Obviously, Congress intended only that the Secretary of Labor be authorized to determine the prevailing wage, and from this it would naturally follow that adverse effect was to be determined on the basis of prevailing wage. This is a far cry from the determination and enforcement of a "wage necessary to prevent adverse effect".

Also convincing in regard to Congressional intent is the amendment which was proposed in *H. R. 12176,* as shown in House of Representatives Report 1642 dated May 23, 1960. The Brief Summary of H. R. 12176 is:

> "H.R. 12176 would accomplish two simple purposes as follows:
>
> "1. To extend the authorization of the Mexican farm labor program for an additional 2 years, until June 30, 1963.
>
> "2. To clarify the intent of Congress by providing that neither title V of the Agricultural Act of 1949 nor the Wagner-Peyser Act of 1933 is intended to serve as a vehicle for the regulation of wages, hours, or perquisites of domestic farmworkers."

The proposed amendment was:

> "Nothing in this Act nor in the Act of June 6, 1933 (48 Stat. 117), shall be construed to confer any authority upon the Secretary of Labor to regulate the wages, hours, perquisites, or other conditions of employment of domestic farmworkers."

In dealing with this amendment the Majority Report outlines the history and the policy of the Act of June 6, 1933 (48 Stat. 117), which is the Wagner-Peyser Act. The Report stated the position of the majority of the Committee that the Department of Labor had, through its rule-making authority in administering the Wagner-Peyser Act, undertaken to regulate wages and working conditions of domestic labor contrary to the intent of Congress. The Report concluded:

> "The committee asserts a belief that executive interpretation of general language of an act to au-

thorize doing what Congress did not intend be done is a practice inconsistent with constitutional intent and purpose and involving usurpation of a responsibility of the Congress.

"The committee feels that the issue involved is not the motives behind or reasonableness of the regulations issued by the Secretary of Labor. The basic issue is whether, within the framework of our constitutional form of government, it is for the Congress or for the executive branch to legislate in this important area of the law.

"The committee believes that if such regulatory authority is to be exercised by the Federal Government, this should be done only after proper legislative process and affirmative action by the Congress.

"Whatever anyone may believe the Congress should do in this connection, the inescapable fact is that the Congress has not done so; and until Congress chooses to do so by specific congressional enactment, it is a violation of sound governmental practice for an executive agency to proceed without such specific mandate.

"The bill reported by the committee would establish what, in its opinion, has always been the congressional intent, that the Wagner-Peyser Act is not to be construed to authorize the regulation of wages, hours, or prerequisites provided farmworkers."

Thus we submit that the Report and the proposed mendment clearly indicate the expressed opinion of the gricultural Committee that it was never the intention

of Congress to confer on the Secretary of Labor the authority to regulate wages or working conditions in agriculture, either under the Wagner-Peyser Act or under Public Law 78.

H. R. 12176 was never reported out of committee and consequently never came to a vote before the House of Representatives, but the failure to report out the bill and bring it to a vote before the House is clearly explained by Congressman Gathings in the following exchange with Congressman Poage (*Congressional Record June 29, 1960,* page 13901):

> "Mr. Gathings. Mr. Chairman, the Subcommittee on Supplies, Machinery, and Manpower held extended hearings on this legislation. We reported out a bill that bore my name, that was really a committee bill. That legislation had two parts. One incorporated the identical language carried in the Sisk bill which would extend Public Law 78 for a period of 2 years. The other provision was one that had to do with the Wagner-Peyser Act, which was passed by this Congress in 1933, and the regulations that had been promulgated under the provisions of that act by the Secretary of Labor.
>
> It was felt in the dying hours of this Congress that we did not have sufficient time to go into the second version of that legislation, so we deferred action on that until the next session when we would have an opportunity to consider that phase of it.
>
> Mr. Poage. Mr. Chairman, will the gentleman yield?

Mr. Gathings. I yield to the gentleman from Texas.

Mr. Poage. Am I not correct in saying that the subcommittee and later the committee felt that it would be unnecessary and unwise to bring in the additional provisions inasmuch as it was clearly the existing law and that the committee felt that the Secretary had no power to exercise the powers that he claimed to have a right to exercise; and since he had no power, we would be but doing a vain thing to try to say to him that he could not have this power that he did not have.

Mr. Gathings. We recognize that he does not have that power to issue these regulations under the Wagner-Peyser Act since the legislative branch gave no such authority to him.

Mr. Poage. That is right. We all recognize he does not have those powers today. I want it understood that right now we are advising the House that this is a part of the legislative history.

Mr. Bailey. Mr. Chairman, will the gentleman yield?

Mr. Gathings. I yield to the gentleman from West Virginia.

Mr. Bailey. Are we to understand that you are going to put the Secretary of Labor, Mr. Mitchell, on record as being for this legislation?

Mr. Gathings. I am not speaking for the Secretary of Labor.

Mr. Bailey. I am saying that he is not for this legislation.

Mr. Gathings. He may not be and he may be, but he has been supporting it previously.

Mr. Bailey. You are taking away from him authority that he already has.

Mr. Gathings. I will not yield any further to the gentleman. He has assured authority that does not exist. Congress is the legislative branch and it has exempted the farmer from the provisions of the Fair Labor Standards Act and the Landrum-Griffin Act.

Mr. McIntire. Mr. Chairman, will the gentleman yield?

Mr. Gathings. I yield to the gentleman from Maine.

Mr. McIntire. Am I correct in my understanding that the subcommittee that considered this legislation had under consideration the matter of the jurisdiction of the Wagner-Peyser Act, and that after very careful consideration it is the opinion of the subcommittee and the full committee that the Wagner-Peyser Act does not grant to the Secretary of Labor the authority to deny the use of Employment Security offices to farmers unless they comply with such conditions as the Secretary of Labor may wish to impose?

Mr. Gathings. It does not and did not grant him such authority. That is the opinion of the subcommittee and the full Committee on Agriculture. There were only three dissenters on the committee which is composed of 33 members.

Mr. McIntire. The fact that the conditions of the Wagner-Peyser Act are not a part of the legislation now before the Committee does not change the position of the subcommittee in relation to our understanding of the provisions of that act?

Mr. Gathings. Not at all."

Thus it is clearly explained why the proposed amendment was never put to a vote but at the same time it shows the intention of Congress with respect to the limits of the authority of the Secretary of Labor over wages, hours, etc.

Further evidence of the intention of Congress is set forth in House of Representatives Report 274, 88th Congress 1st Session dated May 6, 1963 to accompany H. R. 5497 which was a proposed bill to extend Public Law 78 for an additional two years:

"During the hearings the committee has reviewed evidence regarding the administration of the act by the Secretary of Labor. More particularly, it has considered with great concern the determinations made by the Secretary of Labor under subsection (2) of section 503 of the act. Under this subsection, before any workers are to be made available for employment in any area, the Secretary of Labor must first determine and certify that the employment of such workers will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed.

Purporting to act under this authority, the Secretary of Labor has recently been setting wage rates for Mexican nationals (which also must be paid to domestic workers by the employers of nationals) which he euphemistically calls "the wage rate to prevent adverse effect." The committee has viewed this action with great concern because, under the guise of making a determination relating to the wages of Mexican workers the Secretary of Labor actually is establishing a minimum wage for domestic agricultural labor. Clearly it

was never the intention of Congress to give the Secretary such authority. Congress only intended that he determine adverse effect on the basis of the prevailing wage. The so-called adverse effect wage orders are presently being challenged in the courts, and it is expected that the courts will in due course curb this unwarranted usurpation of power by the Secretary of Labor.

This same matter was considered with considerable concern by this committee in connection with its report on H.R. 12176, 86th Cong. (H. Rept. 1642, May 23, 1960). In that report the committee declared:

> The basic issue is whether, within the framework of our constitutional form of government, it is for the Congress or for the executive branch to legislate in this important area [the regulation of wages and hours] of the law.
>
> The committee believes that if such regulatory authority is to be exercised by the Federal Government, this should be done only after proper legislative process and affirmative action by the Congress.
>
> Whatever anyone may believe the Congress should do in this connection, the inescapable fact is that the Congress has not done so; and until Congress chooses to do so by specific congressional enactment, it is a violation of sound governmental practice for an executive agency to proceed without such specific mandate.

The committee reiterates its position on this matter, and it hereby declares that this recommendation for an extension of the act is not to be con-

strued in any way as condoning or approving the actions of the Secretary of Labor in assuming authority to regulate wages or hours in agriculture."

Another indication of Congressional intent is set forth in *Senate Report 619* dated July 25, 1961. In proposing an amendment to Section 501 the Report sets forth:

"The new section 505 prohibits workers recruited under the act from being made available to, or permitted to remain in the employ of, any employer unless he offers and pays both domestic and foreign workers not less than the prevailing wage paid in the area to domestic workers engaged in similar work. It was not the purpose of the committee to establish minimum wages for farmworkers or to authorize the Secretary of Labor to establish such minimum wages, and the bill does not do so. The establishment of minimum wages falls within the province of the Committee on Labor and Public Welfare, rather than this committee, and employees in agriculture have for good reason been exempted from the minimum wage provisions of the Fair Labor Standards Act."

In conclusion, it is submitted that the legislative history of Public Law 78 and all amendments and proposed amendments thereto establish clearly that Congress intended that the power of the Secretary of Labor should be limited to the determination of the prevailing wage and to the measurement of adverse effect as against the prevailing wage. The legislative history of Public Law 78 indicates clearly that Congress repeatedly expressed its alarm at encroachments made by the Secretary of Labor on the prerogatives of Congress, and repeatedly warned that the Secretary of Labor had no authority to fix wages in agriculture.

III.

IF SECTION 503(2) GIVES THE SECRETARY OF LABOR POWER TO FIX WAGES IT IS INVALID AS DELEGATION OF LEGISLATIVE AUTHORITY WITHOUT SUFFICIENT AND PROPER STANDARDS TO GUIDE THE SECRETARY OF LABOR.

If the court should hold that it was the Congressional intent that Section 503(2) gives the Secretary of Labor the authority to fix or establish a minimum wage, then it is submitted that said law is invalid because it is a delegation of legislative authority, unaccompanied by sufficient standards or expressions of policy to guide and limit the action of the Secretary.

The Constitution provides that all legislative power shall be vested in Congress (U. S. Constitution, Article I, Section 1) and it is axiomatic that Congress may not abdicate its power or delegate its lawmaking functions to an executive or an administrative offer of the government. As expressed by the court in *Schecter v. United States,* 295 U. S. 495, 531, 79 L. Ed. 1570:

> "Congress is not permitted to abdicate or transfer to others the essential legislative functions with which it is thus vested."

There are frequent instances where Congress confers upon the executive or upon an administrative officer the authority to make certain findings of fact, which determine the effective operation of a particular statute, but any such grant of authority must be accompanied

by definite standards to guide the executive or administrative officer in carrying out such functions. As explained by the court in *Schecter v. U. S., supra*:

> "We have repeatedly recognized the necessity of adapting legislation to complex conditions involving a host of details with which the National Legislature cannot deal directly. We pointed out in the Panama Ref. Co. case that the Constitution has never been regarded as denying to Congress the necessary resources of flexibility and practicality, which will enable it to perform its function in laying down policies and establishing standards, while leaving to selected instrumentalities the making of subordinate rules within prescribed limits and the determination of facts to which the policy as declared by the Legislature is to apply. But we said that the constant recognition of the necessity and validity of such provisions, and the wide range of administrative authority which has been developed by means of them, cannot be allowed to obscure the limitations of the authority to delegate, if our constitutional system is to be maintained."

In dealing with the same question the court in the case of *Wichita v. Public Utilities Commission,* 260 U. S. 48, 67 L. Ed. 124 (cited with approval in *Panama Refining Co. v. Ryan,* 293 U. S. 388, 79 L. Ed. 447), held:

> "In creating such an administrative agency the legislature, to prevent its being a pure delegation of legislative power, must enjoin upon it a certain course of procedure and certain rules of decision in the performance of its function. It is a wholesome and necessary principle that such an agency must pursue the procedure and rules enjoined and show a substantial compliance therewith to give validity to its action."

It is conceded that Congress may, under proper circumstances, grant to an executive or administrative officer the authority to make findings or determinations while acting within definitely prescribed limitations of policy set down by Congress, but in the case before the court Congress has not laid down any such standards.

In the case of *Opp Cotton Mills, Inc. v. Administrator,* 312 U. S. 125, 85 L. Ed. 624, the Supreme Court faced the same problem as in the case before this court. The facts of this case were as follows: The Fair Labor Standards Act in its original form set up an administrative procedure for establishing a minimum wage in particular industries, but not in excess of 40¢ per hour, such a wage to be fixed for any industry by the administrator in collaboration with an industry committee. The Act provided that the administrator should from time to time convene an industry committee for each such industry, which committee should recommend the minimum wage or rates of wage to be paid by employers in each industry or classification therein. Upon the administrator's reference to the committee of the question of minimum wage rates in an industry the statute required the committee to investigate conditions in the industry and to recommend to the administrator the highest minimum wage rates for the industry, having due regard to the economic and competitive conditions which would not substantially curtail employment in the industry. The committee was also required to recommend such reasonable classifications within any industry as it determined to be necessary for the purpose of fixing for each classification within the industry the highest min-

imum wage rate. Other specific instructions for the committee were contained in the statute after the industry committee filed its report with the administrator. Later, after due notice to interested persons and giving them an opportunity to be heard, the administrator was required either to approve or disapprove the recommendations, and finally to establish a minimum wage rate. These provisions of the Act were attacked as unconstitutional delegation of legislative authority on the ground that the standards set down by Congress were vague and indefinite. The court held that the Act was valid and did not constitute an unlawful delegation of power.

An analysis of this case and of the Fair Labor Standards Act as it was originally enacted shows clearly the line of demarcation between a lawful grant of authority to an administrative official and an unlawful delegation of legislative power. It is submitted that applying the principles enunciated by this case to the case at hand shows clearly that if Congress intended to grant to the Secretary of Labor the authority to establish and fix a minimum wage, such a grant of authority was invalid because of the failure to fix standards, set definite policies, and prescribe limits.

On the other hand, applying the same principles, it is clear that if Congress intended nothing more than that the Secretary of Labor should determine by an appropriate survey the prevailing wage in each area where Mexican Nationals were to be employed, and on the basis of this prevailing wage determine whether adverse effect would result, such a grant of authority would clearly come within "prescribed limits and the determination of facts which the policies as declared

by the legislature is to apply." *Schecter v. U. S., supra.*

In conclusion, the appellants state unequivocally that they do not believe that Section 503 is unconstitutional. They do believe, however, that the action of the Secretary of Labor in fixing the so-called adverse effect wage was a legislative act. From this it inevitably follows either that the action of the Secretary is invalid under the law, or the law giving him the authority to legislate is invalid. By pleading in their Second Cause of Action the unconstitutionality of Section 503 they intend to point up the issue that either the action of the Secretary of Labor or the Act of Congress is invalid, and they hope to convince the court that it is not Congress, but the Secretary of Labor who stands in error; that Congress did not enact an invalid statute making an unconstitutional delegation of authority —rather the Secretary of Labor exceeded the authority given him by Congress when he issued the adverse effect wage orders.

CONCLUSION.

For the reasons stated it is respectfully submitted that the District Court's order granting summary judgment to the defendants, and refusing to grant injunctive and declaratory relief as prayed for by the plaintiffs should be reversed.

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Certificate.

I certify that in connection with the preparation of this Brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion the foregoing brief is in full compliance with those rules.

IVAN G. McDANIEL,
LEON L. GORDON,

No. 18,838

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

LIMONEIRA COMPANY, ROGER DONLON, PAUL B. KERSTEN, and E. B. ANTONELL, et al.,

Appellants,

v.

W. WILLARD WIRTZ, SECRETARY OF LABOR, and ROBERT C. GOODWIN,

Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA

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IN THE UNITED STATES COURT OF APPEALS
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Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA

JURISDICTIONAL STATEMENT

This action was brought in the United States District Court for the Southern District of California, for the purpose of challenging certain administrative determinations made by the defendants under an act authorizing the importation of Mexican agricultural workers (65 Stat. 119, as amended, 7 U.S.C. 1461, hereinafter called "the Act" or "Public Law 78"). Plaintiffs sought an injunction restraining defendants from proceeding pursuant to these determinations and a declaration that the determinations are beyond defendants' statutory authority under Section 503(2) of the Act (R. 9). In the alternative, plaintiffs sought a judgment declaring that, if such deter-

minations are authorized by Section 503(2), then such Section is unconstitutional as an unlawful delegation of legislative power (R. 9).

This appeal is taken from a judgment entered June 10, 1963, granting summary judgment to defendants.

The jurisdiction of the district court was asserted on the basis of 28 U.S.C. 1331, 1332 and 1337.[1] The jurisdiction of this Court is based on 28 U.S.C. 1291.

STATEMENT OF THE CASE

1. Introduction. Public Law 78 authorizes, under certain conditions, the recruitment and importation into the United States of Mexican agricultural workers (commonly known as "braceros").[2] Section 503 provides that none of these imported workers shall be available for employment in any area unless the Secretary of Labor has determined and certified that, among other things,

> the employment of such workers will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed

Article 10 of the Migrant Labor Agreement of 1951, as amended -- an agreement negotiated with the Republic of Mexico pursuant to the provision in the Act (Section 501)

1 / We dispute (see infra pp. 7-25) the existence of a justiciable case or controversy. Thus, we dispute the existence of any jurisdiction in the court below.

2 / Public Law 78 expires December 31, 1963. See 75 Stat. 761, amending 7 U.S.C. 1470. A bill providing for a one-year extension, with no other amendments, passed the House of Representatives October 31, 1963. 109 Cong. Rec. 19685 (daily ed.). The Senate passed a bill providing for a one-year extension and another amendment, requiring that domestic workers be offered insurance coverage, housing, transportation and a work period guarantee comparable to those offered the Mexican workers. 109 Cong. Rec. 14404 (August 15, 1963, daily ed.). The matter is now in conference. This case will, of course, be moot if no extension is passed. It is not believed that the Senate amendment would affect this case.

that the importation of workers be "pursuant to arrangements between the United States and the Republic of Mexico"--provides that only employers obtaining the required certification may employ Mexican workers under the Act. Articles 9(a) and 15(a) of the Migrant Labor Agreement require the employer to pay the wage rate determined by the Secretary of Labor to be necessary in order to permit him to certify that employment of Mexican workers will not adversely affect domestic wages and working conditions.

Two determinations are challenged by this action. The first is set forth in a letter, dated March 29, 1962, from defendant Goodwin, who is the Administrator of the Bureau of Employment Security of the United States Department of Labor, to all state employment security agencies (R. 11). The second is set forth in a memorandum dated October 19, 1962, from defendant Goodwin to certain Regional Administrators of the Bureau of Employment Security (R. 13). Both determinations announced that defendants would be unable to certify that employment of Mexican agricultural workers in the States specified in the determinations will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed unless the Mexican workers are paid certain specified hourly wage rates or equivalent piece rates. It was further announced that employers could not be authorized to employ such workers under the Act unless they paid such workers the specified rates.

2. The Complaint. Appellants herein (plaintiffs below) allege that they are users of Mexican workers under the Act and that this action is brought for themselves and on behalf of all users of Mexican agricultural workers (R. 3). It is alleged that plaintiffs "are partially or wholly dependent" on the use of Mexican labor imported under the Act in the production and harvesting of their crops (R. 4). It is further alleged that defendants' action in making the challenged determinations "has deprived the Plaintiffs of their right to negotiate a wage and to determine the manner of payment, whether an hourly rate or piece rate, with Mexican National agricultural workers, in accordance with the provisions of [Section 501(5)] of the Act." (R. 7). Section 501 (5) of the Act provides that the Secretary of Labor is authorized:

> (5) to assist such workers and employers in negotiating contracts for agricultural employment (such workers being free to accept or decline agricultural employment with any eligible employer and to choose the type of agricultural employment they desire, and eligible employers being free to offer agricultural employment to any workers of their choice not under contract to other employers).

No allegation is made as to whether plaintiffs are in fact paying wages below the rates specified in the challenged determinations, whether defendants have at any time threatened to withdraw plaintiffs' authorization to employ Mexican workers under the Act on the ground that their wages have been below those specified in the determinations, whether plaintiffs were paying such workers at rates below those specified in the determinations before they were issued, or whether plaintiffs would pay rates below those specified in the determinations if they are revoked or declared null and void.

It is, however, alleged generally that each of the plaintiffs "is adversely affected by the actions of the Defendants in making . . . promulgating, maintaining and enforcing" the challenged determinations, and that each of the plaintiffs "will suffer as a result of said wrongful action irreparable damage in an amount in excess of Ten Thousand Dollars ($10,000), exclusive of interest and costs." (R. 8).

The first challenged determination stated that an adverse-effect certification would not be made for Mexican workers employed at hourly wage rates lower that $1.00 an hour in California (R. 11). This determination is dated March 29, 1962, and took effect immediately. Exhibit D to defendants' motion for summary judgment (R. 130) is a table prepared by the California Department of Employment from the California Weekly Farm Labor Report. This table compares "commonly reported hourly wages" by county for the year prior to March 29, 1962, and the year after March 29, 1962. For Ventura County, in which the plaintiffs Limoneira Company and Roger

Donlon are alleged to be engaged in the business of raising citrus fruit and miscellaneous vegetable crops (R. 2), the table states that the commonly reported hourly wage in both years was $1.00 an hour. For Kern County, in which plaintiff E. B. Antonell is alleged to be engaged in the business of raising miscellaneous vegetable crops (R. 3), the table states that the commonly reported hourly wage in both years was $1.00 an hour. For Riverside County, in which plaintiff Paul B. Kersten is alleged to be engaged in the business of raising miscellaneous row crops (R. 2-3), the table stated that the commonly reported wage was the same in both years -- $1.00 an hour -- for the western part of the county, but that in the eastern part it was $.85 an hour for the year prior to March 29, 1962, and $1.00 an hour for the year after.[3/]

The second challenged determination (R. 13) stated that an adverse-effect determination would not be made for lettuce ground harvest unless the Mexican workers were paid the higher of a specified piece rate or the "adverse effect" wage rate for the state in question-- which was $1.00 an hour in the case of California. This determination was dated and took effect on October 19, 1962. Exhibit E to defendants' motion for summary judgment is a collection of tables, entitled "Piece Rate Earnings of Mexican Nationals Employed in California, January 1 through

3/ The record is not clear whether Mr.Kersten's farm is located in the eastern or western portion of Riverside County. The record does show, however, that Mr. Kersten employs no more than 90 braceros (R. 155).

December 31, 1962," prepared by the Bureau of Employment Security of the Department of Labor. Table VI (R. 146) states the average wage per hour by county and crop. In Ventura County, the average for lettuce harvest was $1.23 an hour. No figure is given for lettuce harvest in Kern County. For Riverside County (East) for figure given is $1.36 an hour; no figure is given for lettuce harvest in Riverside County (West).

3. Background of the Challenged Determinations.

The administrative experience under the Act which led to issuance of the determinations here challenged was recounted by Secretary (now Justice) Goldberg in testimony given on June 13, 1961, at hearings held by the Subcommittee on Agricultural Research and General Legislation of the Senate Committee on Agriculture and Forestry, 87th Cong., 1st Sess. (the printed transcript of these hearings is hereinafter referred to as the "Hearings"). The Subcommittee was considering a number of bills in connection with the proposed extension of the Mexican farm labor program to December 31, 1963, and Secretary Goldberg was explaining the Administration's position.[4/]

Secretary Goldberg explained that "tremendous difficulty" was encountered in administering the "adverse effect" provision and the provision of Section 503(3) that no workers be available for employment under the Act unless the Secretary has determined

4/ The major portion of Secretary Goldberg's testimony was in the form of a prepared statement, which is reprinted at 107 Cong. Rec. 18783-18787 (September 8, 1961).

and certified that

> reasonable efforts have been made to attract domestic workers for such employment at wages, standard hours of work, and working conditions comparable to those offered to foreign workers.

(Emphasis added.) As Secretary Goldberg pointed out, the intent of these two provisions was that the available domestic labor should be hired at a rate unaffected by the importation of Mexican workers, and that Mexican workers could then be hired when necessary to supplement the domestic labor force. Hearings, pp. 229-30.[5/]

As appellants point out, the practice followed in the first few years of administering Section 503 was to certify that no adverse effect would occur if the imported foreign workers were paid the prevailing wage rate offered domestic workers for similar work in the area into which the braceros were imported. This was believed at the time to be sufficient to satisfy the intent of the program as one of supplying foreign workers to supplement, rather than to replace, the domestic labor force. In any area in which the foreign workers were merely supplementary, the idea was that the prevailing wage rate would be set by the supply and demand for domestic labor, and employment of supplemental foreign labor would not adversely affect the wages of domestic labor. Hearings, pp. 229-30.

However, as years of experience in administering the Act accumulated, the Labor Department found that in many areas Mexican workers were replacing domestic labor and either

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5/ See Senate Report 214, 82d Cong. 1st Sess., U.S. Code Congressional and Administrative News, p. 1569: "your committee belives that provision should be made at this time for supplying the foreign agricultural labor found necessary to supplement the domestic labor force" (Id. at 1572).

driving down the prevailing rate for the area or preventing it from rising in accordance with the general nationwide rise in agricultural wage rates. Hearings, pp. 165,230.

For example, as Secretary Goldberg explained, 123 wage surveys made in 1960 in areas employing braceros revealed that in 67 per cent of the cases the wage paid domestic workers was the same as in the previous year despite generally rising farm wages, while in 15 per cent of the cases the wage paid domestic workers had actually declined. It was also found that in Arkansas, Missouri, Texas, and New Mexico the wage rate normally paid Mexican workers in 1960 -- 50 cents per hour -- was the same rate paid in 1951, when the Act first went into effect.[6/] Since growers were required to pay Mexican workers the prevailing rate offered domestic workers, and since domestic workers had only to be offered the rate paid the Mexicans, it is apparent that any domestic agricultural workers left in these states were also failing to participate in the general rise in agricultural wage rates. Hearings, pp. 165, 230.

An attempt was made to remedy this situation, which was felt to be a subversion of the congressional intent, expressed in Section 503(2), to prevent the Mexican labor program from adversely affecting wages of domestic agricultural workers. After a few isolated earlier efforts, in 1958 the Secretary adopted a policy that piece work rates should produce not less than 50 cents an hour for reasonably diligent workers. This

6/ The results of these and other similar surveys are summarized at 107 Cong. Rec. 7727 (May 10, 1961).

resulted in the so-called 90/10 formula: 90 per cent of the workers must make each week at least 50 cents an hour, provided that, if more than 10 per cent of the workers average less than 50 cents an hour, the employer might prove that such workers were incompetent. Hearings, p. 231. Initially an attempt was made to obtain compliance with this policy on a largely voluntary basis, but with little success. Hearings, p. 165. Then on May 17, 1960, the Secretary announced a determination that he could not certify that employment of Mexican workers at a wage of less that $2.50 per cwt. for picking cotton, or such higher rate as necessary to achieve a rate of 50 cents an hour in accordance with the 90/10 policy, would not adversely affect the wages and working conditions of domestic workers similarly employed. The Department conceded that this determination was not based upon the prevailing domestic wage rate for the areas involved.

This determination was promptly challenged in the courts. Johnson v. Kirkland, 290 F. 2d 440 (C.A. 5), certiorari denied 368 U.S. 889; and Rio Hondo Harvesting Ass'n v. Johnson, 290 F. 2d 471 (C.A. 5). Decisions favorable to the Secretary were obtained in the spring and summer of 1961. During the period of over a year in which the cases were being litigated, the Secretary was enjoined from putting the determination into effect, and the Mexican workers in the areas involved generally received less than 50 cents an hour. Hearings, p. 231. The decisions in favor of the Secretary were based wholly on procedural grounds

and thus did not settle the substance of the legal dispute.

Faced with frustrating and inconclusive litigation and with continuing attacks in both Congress [7] and the courts [8] on his authority under Section 503, in 1961 the Secretary sought legislation. The Secretary made it clear that he believed the administrative actions which had resulted in the Johnson and Rio Hondo cases were authorized by Section 503(2) in its present form, but that additonal legislation was desirable to avoid further litigation. Hearings, p. 165-66. The bills supported by the Admisistration -- S. 1945 and H.R. 6032, 87th Cong., 1st Sess. -- specified that employers using Mexican workers would be required to offer them the statewide or national average rate for hourly paid farm labor, whichever is less, with the proviso that no employer would be required to increase his rate by more than 10 cents an hour in any year. The proposal was approved by the Senate (107 Cong. Rec. 18902 (September 11, 1961)), rejected by the House (107 Cong. Rec. 7726 (May 10, 1961)), and finally rejected in conference (107 Cong. Rec. 19796 (September 16, 1961)). [9]

7/ See legislative history quoted in Appellants' Brief at pp. 48-53.

8/ Dona Ana County Farm & Livestock Bureau v. Goldberg, 200 F. Supp. 210 (D.D.C.).

9/ The bill which was approved by the Senate and went to conference was an amendment offered from the floor by Sen. McCarthy, requiring that the Mexican workers be paid at least 90 percent of the national or state average, whichever is less. No provision limiting the required annual raise to 10 cents an hour was included. 107 Cong. Rec. 18770 (September 8, 1961). The bill initially rejected by the House was H.R. 6032, which provided as stated in the text.

The legislative history does not reveal any single reason for the rejection. Some Senators and Congressmen thought that the Secretary should not be given authority to set minimum wages in the manner specified. See 107 Cong. Rec. 7707 (May 10, 1961) (Rep. Sisk); 107 Cong. Rec. 18901 (September 11, 1961) (Sen. Cooper). Others thought the present law gave the Secretary sufficient power to prevent adverse effect. 107 Cong. Rec. 7726 (May 10, 1961) (Rep. Teague); 107 Cong. Rec. 7714 (May 10, 1961) (Rep. Cooley). Others interpreted the proposed bill as requiring or having the effect of an annual wage escalation each year and objected to the provision on this ground. See 107 Cong. Rec. 7727 (May 10, 1961) (Rep. Gathings); 107 Cong. Rec. 18803 (September 8, 1961) (Sen. Jordan). Secretary Goldberg himself reported to the Senate Subcommittee that opposition had arisen on the ground that the bill was not needed because the authority for establishing the wage formula specified in the Administration bill existed under the present statute. Hearings, p. 230.

Secretary Goldberg made it quite plain to the Senate Subcommittee that he believed he had the authority under Section 503(2) to establish a minimum wage along the lines of the formula specified in the Administration bill, and that additional legislation was being sought for the purpose of clarification of standards and avoidance of litigation, rather than for the purpose of conferring authority which did not otherwise exist. Hearings, pp. 165-66. This view was reiterated by Senator Mansfield on the floor of the Senate, 107 Cong. Rec. 18899

(September 11, 1961). The Department's view of its authority under Section 503(2) was also well known to the House. See legislative history quoted in App. Br. 48-52. And yet, despite extensive consideration of the whole Mexican labor program by both Houses of Congress -- including consideration of several amendments made in committee and offered from the floor[10/] -- no one proposed a bill specifically to deny the Secretary the authority over wages which he claimed to possess under Section 503(2), although such a bill had been proposed at the previous session and had failed to get to the floor of the House, according to its sponsor, only because of lack of time (App. Br. 50). The reason for this failure may well have been the attitude of the Senate; in view of its vote in favor of the Administration-backed bill, the Senate could hardly have been expected to approve a bill denying the Secretary the authority he claimed to possess.

In any event, this legislative impasse left the Secretary in the position he had been in before proposing new legislation. In his statement upon signing the bill extending the program to December 31, 1963, the President expressed his dissatisfaction with the failure of Congress to include the Administration-backed amendments and noted that the program as then administered was adversely affecting wages and working conditions of domestic agricultural workers. Referring to the "comprehensive, general

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10/ Five days of hearings were held by the Subcommittee on Equipment, Supplies and Manpower of the House Committee on Agriculture, from March 6-17, 1961. Two days of hearings were held by the Subcommittee on Agricultural Research and General Legislation of the Senate Committee on Agriculture and Forestry, on June 12 and 13, 1961. House debates are reported at 107 Cong. Rec. 7706-28 (May 10, 1961), 7869-72 (May 11, 1961). Senate debates are reported at 107 Cong. Rec. 18767-92 (September 8, 1961), 18803-6 (September 8, 1961), 18899-906 (September 11, 1961).

authority" of the Secretary under Section 503(2), the President went on to say:

> I sign this bill with the assurance that the Secretary of Labor will, by every means at his disposal, use the authority vested in him under the law to prescribe the standards and to make the determinations essential for the protection of the wages and working conditions of domestic agricultural workers. 11/

The Secretary proceeded to obtain the agreement of the Mexican Government to an appropriate amendment to the Migrant Labor Agreement of 1951 (App. Br. 5, 18-22). The determinations challenged in this action were then proposed and, after public hearings, were made and issued.

4. Proceedings Below. On defendants' motion for summary judgment, the district court held that (1) the challenged determinations were within the Secretary's authority under Section 503, and (2) there was no substantial question warranting a three-judge court as to the constitutionality of Section 503 (plaintiffs having requested a three-judge court under 28 U.S.C. 2282 to rule on the question of constitutionality in the event that the determinations were held to be authorized by Section 503 (R. 51)).

As to the question of statutory authority, the district court, after reviewing the authorities, had this to say (R. 186):

> It is extremely difficult to follow the plaintiffs' argument that unless the "braceros" are paid the prevailing wage their employment will adversely affect the domesti workers, but the Secretary cannot say that unless a certain wage, which is concededly reasonable, is paid the "braceros the domestic worker would be adversely affected.

11/ Public Papers of the Presidents, John F. Kennedy, 1961, at pp. 639-40.

> True, the latter basis might have the indirect effect of fixing wages for domestic workers in areas where "braceros" are employed, but certainly the employment or threatened employment of "braceros" might well cause a depressant effect upon prevailing wages and, thus, an "adverse affect." The "adverse affect" is what the statute is designed to prevent, and the fixing of a minimum wage rate would appear to be a much more effective means of preventing an "adverse affect" than using the prevailing wage rate as a criteria.

As to the question of constitutionality, the district court reasoned as follows (R. 180):

> Plaintiffs conceded in their argument that if the Secretary confined his findings of "adverse affect" based upon prevailing wages rather than upon minimum wages, there could be no claim of unconstitutionality. Inasmuch as it is found that there are no grounds for distinction, there can likewise be no claim of unconstitutionality.

STATUTE INVOLVED

Public Law 78, as amended, is set forth at pp. 7-13 of Appellants' Brief.

SUMMARY OF ARGUMENT

I. This case has not ripened into a justiciable case or controversy in which the statutory and constitutional questions urged by plaintiffs may be adjudicated, for the following reasons: (1) plaintiffs have not shown that they will or are likely to pay wages below the level specified in the Secretary's determinations, (2) there has been no threat to enforce the policy expressed in the

determinations against plaintiffs by withdrawing their authorizations to employ braceros, or by refusing to issue authorizations in the first instance, or by any other means, and (3) aside from general allegations of damage, which are rebutted by such facts as have been put before the court below, there has been no allegation or showing that the mere existence of the Secretary's determinations has damaged plaintiffs by causing them to pay wages higher than what they would otherwise pay.

II. The command of Section 503(2) of the Act, that employment of braceros shall not adversely affect the wages of domestic workers, is a fundamental part of congressional purpose in establishing the Mexican labor program. Thus, when the Secretary found that employment of braceros was adversely affecting the prevailing wage paid domestic workers, it was his duty under Section 503(2) to condition his adverse effect certifications on payment of another wage level which would not have a depressant effect on the prevailing domestic wage. The two determinations here challenged are an attempt to carry out this duty -- an attempt which was not only authorized by the Act, but was indeed required in light of the effect the program was having on prevailing domestic wages.

III. Section 503(2) does not give the Secretary a roving license to set minimum wages at any level he may desire. On the contrary, it lays down a standard -- adverse effect on domestic wage rates -- which under

applicable precedent is sufficiently specific to sustain the delegation of wage-setting authority made by the Section.

ARGUMENT

I. This case has not ripened into a justiciable controversy within the jurisdiction of the district court.

While the Secretary is anxious to have a ruling on the merits of this case, we feel compelled to point out to this Court that, in its present posture, the case has not ripened into a justiciable "controversy" within the meaning of the Declaratory Judgments Act, 62 Stat. 964, as amended, 28 U.S.C. 2201, and Article III, Sec. 2 of the Constitution.

The reason for this is quite simple. Plaintiffs have not alleged that they are paying, have paid, or intend to pay wages below the levels set forth in the Secretary's determinations. Nor have they alleged that the Secretary has threatened to enforce the determinations by revoking their authorizations to employ Mexican workers under the Act. And finally, they have not alleged that compliance with the determinations, or the existence of the determinations, has in any way damaged their businesses by requiring them to pay wages above what they would otherwise pay. The general allegations that

plaintiffs are "adversely affected" and "will suffer . . . irreparable damage" (R. 8) are not sufficient to establish justiciability, especially in the face of statistics offered by defendants casting serious doubts on the existence of any substantial damage. And the allegation that plaintiffs have been deprived of some abstract "right to negotiate a wage" (R. 7) is insufficient without a more specific allegation as to some concrete interference with the supposed right.

As Mr. Justice Frankfurter has pointed out, "Justiciability is, of course, not a legal concept with a fixed content or susceptible of scientific verification." Poe v. Ullman, 367 U.S. 497, 508. Accordingly, the decisions which define and apply the concept may not always have been perfectly consistent. However, the Supreme Court decisons have all required that at least one of the following elements be present to establish justiciability: (1) plaintiff is about to engage in conduct running afoul of the statute or administrative action sought to be challenged, (2) such statute or action is about to be enforced against him, or (3) in certain extraordinary circumstances, the mere existence of such statute or action has caused him substantial damage. None of these elements is present here.

1. Perhaps the closest precedent on its facts to the instant case is Communist Party v. Control Board, 367

U.S. 1, in which a challenge to certain statutory provisions was held to be nonjusticiable because the Court doubted that the petitioner would ever engage in conduct running afoul of the challenged provisions. In that case petitioner challenged a statute requiring it to register and attaching certain disabilities to its operation after registration -- depriving it of a tax exemption, requiring that it label any mailed propaganda, denying passports to its members, making its members ineligible for federal employment, subjecting its alien members to deportation, and so on. Since the case arose as an appeal from an order requiring petitioner to register, there was no doubt that the Court was required to adjudicate questions pertaining to the provision requiring registration. However, the Court refused to adjudicate the challenge to the provisions imposing disabilities on registered organizations, on the ground that it did not know that petitioner, once registered, would ever engage in activities affected by the statutory disabilities. For example, the Court did not know that petitioner would have any taxable income, would mail any material required to be labeled, would have any member seeking a passport or a federal job, or a would have any alien member subject to deportation under the statute. 367 U.S. at 78-79.[12/] The Court found to be controlling a case in which it had refused to find

12/ Of the four dissenters, only one disagreed with the Court's conclusion on this point (367 U.S. at 144-45), while two explicitly agreed (367 U.S. at 191) and the fourth limited his discussion of the merits to the registration requirement (367 U.S. at 175).

justiciability on closely similar facts -- Electric Bond & Share Co. v. Securities and Exchange Comm'n, 303 U.S. 419, discussed in 367 U.S. at 73-77 (involving registration under the Public Utility Holding Company Act).

The instant case is governed by the Communist Party and Electric Bond & Share cases. As in those cases, we do not know that the plaintiffs here will ever engage in conduct which will bring into effect the sanction envisaged by the challenged determinations. Indeed, in view of the wage statistics attached to defendants' motion for summary judgment (see supra at pp. 5 - 7), there is affirmative reason to doubt that plaintiffs will ever engage in such conduct. Only in the western part of Riverside County were the wages for the year before the first challenged determination apparently lower than for the year after: 85 cents an hour before, as opposed to $1.00 an hour after (R. 130). Plaintiff Kersten resides at Indio, in the middle of the County (R. 2-3), and was authorized to employ 90 braceros (R. 155). The record does not show in what portion of Riverside County Mr. Kersten has his farm. Therefore, as far as this record shows, Mr. Kersten, along with all the other plaintiffs, has been employing braceros in an area where the prevailing wage has been $1.00 an hour all along. Moreover, neither Mr. Kersten nor any of the other plaintiffs has asserted that he intends in the future to pay wages below the level determined by the Secretary. The reason for this

lack of an essential allegation is, we believe, clear from the fact that the prevailing wage in their areas has been at that level all along.

The figures with respect to lettuce harvest are even more revelaing. The hourly average for the year in which the lettuce harvest determination went into effect was $1.23 in Ventura County (R. 146), and $1.36 in Riverside County (East) (R. 150). And yet the hourly minimum set by the challenged determination was $1.00. These figures at the very least raise a question as to whether the plaintiffs located in these counties can be expected to pay wages for lettuce harvest below the minimum specified in the determination.

2. The Communist Party and Electric Bond & Share cases may be said to represent the most liberal interpretation of the justiciability concept. For they might be read to imply that the issue of justiciability turns in part on whether the party seeking to invoke jurisdiction can show that it will engage in conduct violating the statutory or administrative provision sought to be challenged, and that a treat of immediate enforcement of the provision against the plaintiffs may not be necessary. In other cases the Supreme Court has refused to find justiciability despite the fact that the plaintiffs intended to and could be expected to engage in conduct violating the challenged provision, on the ground that there was no threat of immediate enforecment. United Public Workers v. Mitchell,

330 U. S. 75; Longshoremen's Union v. Boyd, 347 U.S. 222. Of course, no immediate threat of enforcement exists in the instant case. No one has threatened to withdraw plaintiffs' authorizations to employ braceros, or not to issue authorizations which plaintiffs may need, or to enforce the challenged determinations against plaintiffs in any other fashion. The reason, of course, is simple: plaintiffs have apparently not paid wages below the level set in the Secretary's determinations, nor even stated an intention to do so.

The Boyd case is especially noteworthy, since it concerned a complaint closely similar to the instant complaint: plaintiff sought a declaration accompanied by appropriate injunctive relief that an announced administrative determination was beyond the scope of the pertinent statute, and in the alternative requested a ruling by a three-judge court that, if such determination was within the statute, then the statute was unconstitutional. The Court found that there was no justiciable controversy, despite the fact that plaintiff's members not only wished to engage in conduct which would bring into effect the announced administrative sanctions, but had regularly engaged in such conduct in the past--neither of which factors is alleged to be present in the instant case.

3. The Boyd and Mitchell cases would require an immediate threat of actual enforcement before a statute or administrative determination may be challenged. The more recent case of Poe v. Ullman, 367 U.S. 497, appears

also to insist on that requirement.[13] Other cases have been somewhat more liberal, permitting the challenge in the absence of a threat of immediate enforcement where there are detailed allegations that the very existence of the challenged statute or regulation has caused the plaintiff substantial damage. E.g., Columbia Broadcasting System, Inc. v. United States, 316 U.S. 407, in which petitioner alleged that the challenged administrative regulations had caused the cancellation of several contracts which were vital to its operation. Accord: Pierce v. Society of Sisters, 268 U.S. 510; see Communist Party v. Control Board, 367 U.S. 1, 79-81 (citing cases). Cf. California Comm'n v. United States, 355 U.S. 534, in which it was clear that the challenged administrative determinative determinations would substantially impede plaintiff's operations.

In the instant case, all we have is a generalized allegation of damage, which is called into serious question by the wage statistics submitted by defendants. As has been shown, these statistics indicate that in all relevant areas, with the possible exception of Riverside County (East), wage rates for braceros have been generally unaffected by the Secretary's determinations. It may be that plaintiffs could have convinced the court below

13/ Cf. Evers v. Dwyer, 358 U.S. 202, involving a challenge by a Negro to a Tennessee statute requiring segregated seating on buses. Justiciability was predicated on the fact that plaintiff had violated the statute in the past and had been threatened with arrest by two police officers. Clearly, also, the mere existence of the statute damaged plaintiff in the sense that it prevented him from doing what he could and clearly would otherwise do. Both these elements of justiciability -- a threat of enforcement and damage -- are lacking in the instant case.

that defendants' statistics are invalid as applied to plaintiffs' operations. But plaintiffs neither brought forth nor alleged any facts which would so indicate. In these circumstances, general allegations of damage such as those made by plaintiffs clearly would not be sufficient to establish damage for the purpose of jurisdictional amount under 28 U.S.C. 1331 or 1332. KVOS, Inc. v. Associated Press, 299 U.S. 269; McNutt v. General Motors Acceptance Corp., 298 U.S. 178. It is difficult to see how such allegations can be held sufficient for purposes of the more fundamental requirement of justiciability.

Of course, the statutory right which plaintiffs claim to unfettered negotiation with their Mexican workers (R. 7) no more confers justiciability than did the supposed constitutional right of the federal employees in United Public Workers v. Mitchell, supra, to engage in the political activity forbidden by the Hatch Act. Plaintiffs have not alleged an actual or threatened interference with the claimed right, other than such interference as may flow from the mere existence of the administrative determinations they seek to upset. Neither have plaintiffs sufficiently alleged that the mere existence of such determinations has caused them any substantial damage. A justiciable case or controversy does not exist; the action should accordingly have been dismissed for lack of jurisdiction.[14/]

14/Although the district court did not decide the question of justicability, the issue of equitable jurisdiction of the court was raised below (R. 21-22). Of course, the question of justiciability, going to jurisdiction, may be raised any time. See Muskrat v. United States, 219 U.S. 346; Mitchell v. Maurer, 293 U.S. 237, 244.

II. The Secretary's determinations here challenged are attempts to carry out his statutory duty of insuring that employment of braceros does not adversely affect wages of domestic workers. This duty cannot be discharged merely by insuring that braceros are paid a prevailing wage which has been adversely affected by the very fact that braceros are available.

Subsections (1) and (2) of Section 503 are a fundamental part of Public Law 78. Under these subsections, braceros may not be employed unless the Secretary of Labor has certified that (1) sufficient domestic workers who are able, willing and qualified are not available,[15/] and (2) employment of foreign workers "will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed."

The basic concept was that Mexican workers would be available only where there was a shortage of domestic workers. It was thought that the Mexican workers would be only a supplemental labor force. See Senate Report 214, 82d Cong. 1st Sess., U.S. Code Congressional and Administrative News, pp. 1569, 1572. Accordingly their use would not adversely affect domestic workers as long as available domestic workers were first offered the jobs at prevailing wages set without reference to the fact that Mexicans would become available if domestic workers did not accept the wages offered. Thus Senator Ellender, the proponent of the bill which became the original Act (S. 984, 82d Cong., 1st Sess.), referred to Section 503

15/ Under Subsection (3), domestic workers need only be offered the rate paid the braceros. Thus the Secretary's certification is as to availability of domestic workers at the wage rates offered braceros.

in defending the bill against the criticism of Senators Chavez and Lehman, who thought that it would depress the wages of domestic agricultural workers. 97 Cong. Rec. 4476-77 (Sen. Lehman), 4478-79 (Sen. Chavez), 4483-84 (Sen. Chavez) (April 27, 1951), 4513 (Sen. Chaez) (April 30, 1951). Senator Ellender quoted Section 503(1) and (2) in full and went on to say (97 Cong. Rec. 4513-14 (April 30, 1951)):

> Surely . . . if the administrator of this measure does his duty American farm workers will be protected.

Later, Section 503 was used to defend the Act in its present form as attempts were made to strengthen the protection of domestic workers. Congressmen who pointed to statistics showing depressed prevailing wages for domestic labor in areas where Mexican labor was prevalent were told that their remedy did not lie in legislative amendment. It was said that their complaint should be taken to the Secretary of Labor -- that if the Secretary performed his duty under Section 503 as presently written, the Mexican labor program would not depress domestic wages. 107 Cong. Rec. 7714 (May 10, 1961) (Rep. Cooley).

The determinations here challenged are an attempt by the Secretary to perform his duty under Section 503. As pointed out by appellants (App. Br. 4), it was thought during the first several years of the program that this duty could be adequately discharged by conditioning the certifications under Section 503 upon payment of domestic wages prevailing in the area in which the braceros were

to be employed.[16] But, as administrative experience under the program accumulated, it became apparent that this was not sufficient to fulfill the congressional purpose. See Hearings, pp. 164-5, 229-30. Wage surveys taken in 1960 showed that, despite generally increasing agricultural wages, in 67 percent of the areas in which employment of braceros was prevalent, the prevailing wage had remained stationary, while in 15 percent of such areas the prevailing wage had actually gone down. Ibid. Wages paid braceros in Arkansas, Missouri, Texas and New Mexico had remained at 50 cents an hour in the years since 1951. Wages of domestic labor similarly employed in these areas a fortiori were the same, despite a general increase in domestic agricultural wages of 46 per cent in that period. Ibid.

16/ The 1955 amendment to Section 503 (see App. Br. 34), which authorizes provision for obtaining facts relevant to wages paid domestic farm workers, was intended to assist the Secretary in performing his duty under Section 503(2) in the manner that was then thought would adequately carry out the basic purpose of the Section. The 1955 amendment can hardly be read to provide that the "prevailing wage" standard is the only permissible condition to "adverse effect" determinations under Section 503(2), — especially when it has become clear in the light of subsquently developed facts that this standard, standing alone, is inadequate to fulfill the congressional purpose to protect domestic wages. Payment of prevailing domestic wages has remained one condition for certification under Section 503 (2). See Article 15(a), Migrant Labor Agreement of 1951, as amended. Thus the Secretary is still performing his responsibilities under the 1955 amendment to Section 503.

In the face of this evidence, the Secretary of Labor was compelled to act to prevent subversion of the congressional mandate that domestic wages not be adversely affected by employment of Mexicans. After initial attempts in 1959 to deal with the situation became bogged down in inconclusive litigation (Hearings, pp. 165, 231; see Johnson v. Kirkland, supra) the Secretary attempted to get legislative clarification of the authority, which he believed he already had, to condition his certifications under Section 503(2) upon payment of the statewide or nationwide average for agricultural labor, whichever is less.

Some members of Congress agreed with the Secretary that this authority already existed. See 107 Cong. Rec. 18899 (September 11, 1961) (Sen. Mansfield);[17] statement of Rep. Bailey quoted at App. Br. 52. Others disagreed. See App. Br. 48-55.[18] The Senate passed the Administration bill, 107 Cong. Rec. 18902 (September 11, 1961), but it

17/ Senator Mansfield said, among other things:

> This amendment, rather than conferring authority upon the Secretary of Labor in the area of agricultural wages, is a limitation upon the broad authority he presently has under Public Law 78. Under section 503 of that act he may now prescribe wage criteria, which he finds necessary, in the determination of whether the employment of Mexican nationals in an area will adversely affect the wages and working conditions of our agricultural workers similarly employed. He now has authority to prescribe the same test of adverse effect as is proposed by this amendment.
>
> * * * *
>
> If this amendment is not adopted, let there be no future criticism of the Secretary of Labor if he prescribes similar tests administratively. The Secretary of Labor has advised the Congress that he has found clear indications of adverse effect and will feel constrained in carrying out his statutory responsibilities to take steps beyond those already taken. (107 Cong. Rec. 18899 (September 11, 1961)).

18/ It should be noted that the principal thrust of the

failed in the House and in conference, 107 Cong. Rec. 7727 (May 10, 1961), 107 Cong. Rec. 19796 (September 16, 1961). But despite the Secretary's plainly announced view of his own authority under Section 503(2) as it then existed, Congress in the course of extensive consideration of the Mexican labor program also failed to consider or pass any bill denying the Secretary such authority -- although such a bill had been introduced during the previous session and, according to its sponsor, had failed of passage only because of lack of time remaining in that session (App. Br. 49-50).

Faced with congressional refusal to clarify the procedures to be followed in carrying out Section 503(2), the Secretary, at the direction of the President,[19] proceeded to meet his responsibilities under the Section as written by issuing the determinations here challenged.

Certifications under Section 503(2) were to be conditional

18/cont'd.
legislative history quoted at App. Br. 48-55 is directed at the Secretary's assertion of authority under the Wagner-Peyser Act, 48 Stat. 117, as amended, 29 U.S.C. 49. This Act authorizes the Secretary to set up a national system of employment offices. Under the Act, the Secretary had issued regulations conditioning the use of those offices to obtain agricultural workers upon payment of prevailing wages in the area of employment. 24 F.R. 9367 (November 20, 1959), 20 C.F.R. 602.9. The Wagner-Peyser Act has a nationwide effect and may be argued to have no specific provision which would tie the Secretary's minimum wage setting authority to an "adverse effect" standard. By contrast, the effect of the Secretary's determinations under Section 503(2) is limited to the 1.4 per cent of American farms which employ braceros. 107 Cong. Rec. 7720 (May 10, 1961) (reprinting Department of Labor figures for 1959). Thus the fact that the Secretary's efforts under Wagner-Peyser elicited congressional concern over unwise delegation of authority and possible conflict with the general exemption of agricultural labor under the Fair Labor Standards Act (see App. Br. 37-39) is not a true measure of what congressional reaction would be to the Secretary's present efforts under Section 503(2). It

upon payment of an hourly wage (or equivalent piece rate) at least equal to a specified amount in each state, which the Secretary determined by taking the lower of the statewide average or the nationwide average for hourly agricultural wages. Since the statewide average in California exceeded the nationwide average,[20] the latter average became the applicable standard in California.[21]

This standard was a concession to the growers, since both averages -- especially the statewide average in states bordering on Mexico -- are substantially affected by the presence of braceros on the labor market.[22] Theoretically, the Secretary should have ascertained what the domestic wage level would be if braceros were not on the market and then required that braceros be paid at that rate. This requirement, coupled with the requirement

18/cont'd.
might also be noted that attempts were made in 1960 and in 1961 to amend the agricultural exemption in the Fair Labor Standards Act so as to deny the Secretary authority under the Wagner-Peyser Act to fix minimum wages. These attempts failed. See note 26 infra.

19/ See text at note 11 supra.

20/ See testimony of Assistant Secretary of Labor Holleman, Hearings on H.R. 2010 before Subcommittee on Equipment, Supplies, and Manpower, House Committee on Agriculture, 87th Cong., 1st Sess., at p. 329, in which Mr. Holleman suggested the alternative standard of the nationwide average to deal specifically with the fact that agricultural wages in California are "rather high".

21/ The nationwide average hourly farm wage in 1961, without room or board, as reported by the Statistical Reporting Service of the United States Department of Agriculture in Farm Labor (January, 1962 issue), was $.99.

22/ Statistics on the number of foreign workers as a percentage of total seasonal employment in agriculture for 1960 are reported in the Hearings at p. 209. Nationally the figure was about 20 per cent. In California the figure was about 30 per cent.

in Section 503(3) that no braceros be hired until reasonable efforts have been made to attract domestic workers at the wages offered the braceros, would have afforded domestic workers complete protection from the adverse effect proscribed by Section 503(2). However, lacking any reasonable method of ascertaining exactly what domestic agricultural wages would be in the absence of braceros, the Secretary took for his standard existing state and national averages. Thus, if the Secretary committed any error, it was an error in favor of the growers resulting from the fact that the state and nationwide averages are themselves affected by employment of braceros.

From the foregoing, it is clear that the Secretary's action was not only well within the authority granted him by Section 503(2), but was indeed essential to effectuate the basic congressional intent, expressed in that Section, to protect domestic wages. Thus the case is similar to American Trucking Ass'ns v. United States, 344 U.S. 298, in which comprehensive I.C.C. regulation of motor carrier leasing practices was upheld, despite the absence of specific statutory reference to leasing practices, on the ground that the practices sought to be corrected by the regulations were subverting the regulatory scheme of the Motor Carrier Act. In the instant case Section 503(2) provides much more specific authority than was present in American Trucking, and the evil of depressed domestic farm wages is just as basic to the congressional intent as was the evil of trip-leasing practices at which the reg-

ulations in American Trucking were aimed.

The general principles of statutory construction expounded by appellants (App. Br. 28-31) are unexceptionable. We agree that the power of an administrative official is limited by the statute delegating the power, that an administrative official may not enlarge his statutory powers merely by issuing regulations, and that courts must construe statutes in accordance with the legislative intent and the plain meaning of unambiguous language.

We do not, however, agree with appellants in reading Section 503 to require the Secretary to permit employment of braceros at the prevailing domestic rate when such rate has itself been adversely affected by the growers' knowledge that braceros will be made available if domestic workers do not take the jobs. It must be remembered that domestic workers, under Section 503(3), need only be offered wages comparable to those offered the braceros. All the growers need do under Section 503(3) is to offer domestic workers a rate sufficient to attract braceros if domestic workers do not respond. It is no wonder that in many areas braceros dominate the farm labor force.[23/] To tie the

23/ Hearings, p. 230.

Secretary's "adverse effect" determination to a wage rate which itself has been adversely affected by the presence of braceros on the market is required neither by the plain meaning of Section 503 nor by the congressional intent expressed therein.[24/]

Appellants argue (App. Br. 32) that the plain language of Section 503(2) requires acceptance of their interpretation, however irrational the results, on the ground that the reference in the Section to "the wages and working conditions of domestic agricultural workers similarly employed" must be construed to refer to the domestic wage prevailing at the time of the Secretary's certification in the area where the Mexicans are to be employed. But even if appellants are correct that this reference must be so construed, it is necessary to read the words as part of the sentence in which they occur. The statute says that the "wages . . . of domestic agricultural workers similarly employed" are

24/ At one point, appellants seem to say that the Secretary may "determine whether adverse effect will result" but may not "fix and enforce a wage which will enable him to determine whether adverse effect will result." (App. Br. 33). The implication is that an administrative official may not announce in advance the criteria that will be used in taking specific administrative action, even though the action itself could validly be taken on the basis of such criteria. This implication is plainly contrary to law. National Broadcasting Co. v. United States, 319 U.S. 190 (FCC has authority to regulate network broadcasting by advance announcement of criteria to be used in granting or renewing station licenses). Appellants do not question the Secretary's authority to "fix and determine" the prevailing wage as the "wage which will enable him to determine whether adverse effect will result."

not to be adversely affected. The statute does not say that the Secretary's certification may be conditioned only upon payment to the braceros of the "wages . . . of domestic agricultural workers similarly employed." And indeed, if such domestic wages have been themselves adversely affected by the growers' knowledge that braceros will be available at the depressed domestic rate, then the Secretary would be allowing an adverse effect, and thus failing to carry out what the statute does say, by making the braceros available at the depressed domestic rate.

Appellants also argue (App. Br. 37-39) that Section 503(2) cannot be construed to permit the Secretary to condition his adverse effect certifications on payment of a given level of wages, for the reasor that this construction would repeal by implication the exemption in the Fair Labor Standards Act of 1938 for "any employee employed in agriculture." 52 Stat. 1067, as amended, 29 U.S.C. 213(a)(6). This argument overlooks the fact that Section 503(2) does not give the Secretary a roving license to fix minimum wages, even on the farms on which braceros are employed.[25/] Section 503(2) merely gives the Secretary

25/ The Secretary's determinations only affect farms on which braceros are employed. These farms comprise less than 2% of the total number of farms in the nation. See 107 Cong. Rec. 7720 (May 10, 1961)(reprinting Department of Labor figures for 1959). Thus the overwhelming majority of the farms covered by the agricultural exemption to the Fair Labor Standards Act remain unaffected. It has been pointed out that 52% of American farms use no hired labor of any kind. 107 Cong. Rec. 18900 (September 11, 1961). This point, however, does not alter the fact that the determinations do not substantially affect the agricultural exemption in the Fair Labor Standards Act. It simply means that about 4% of the farms actually using hired

the authority to combat a specific problem that worried Congress -- the adverse effect of braceros on domestic farm wages. This authority can hardly be said to be inconsistent with the general agricultural exemption contained in an earlier statute dealing with a different problem.[26/]

Finally, appellants argue (App. Br. 36-37) that Section 501(5) gives them an unfettered right to negotiate a wage with Mexican workers hired under the Act, subject only to the limitation that it be no less than the prevailing wage. Section 501 provides in pertinent part as follows:

> the Secretary of Labor is authorized --
>
> * * * * *
>
> (5) to assist such workers and employers in negotiating contracts for agricultural employment (such workers being free to accept or decline agricultural employment with any eligible employer and to choose the type of agricultural employment they desire, and eligible employers being free to offer agricultural employment to any workers of their choice not under contract to other employers).

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agricultural labor are presently affected by the determinations -- hardly the sweeping repeal of the agricultural exemption that appellants attempt to portray.

26/ It is interesting to note that in 1960 and 1961 attempts were made to amend the Fair Labor Standards Act to provide that, "Except as may otherwise be expressly provided by law, the Secretary of Labor shall have no power to regulate, either through the withholding of benefits or services or otherwise, the wages of employees employed in agriculture." Both attempts failed. See 106 Cong. Rec. 16500-16521 (August 16, 1960); 107 Cong. Rec. 6256-6259 (April 19, 1961).

All this Section says is that the Secretary shall assist in negotiating the employment contracts, and that the workers are free to choose their employment and the employers are free to choose their workers. If appellants read the Section as prohibiting any limitation on the employment contract not mentioned in the Section, then consistency would require appellants to argue that Article 15 of the Migrant Labor Agreement violates Section 501 by requiring employers to pay the prevailing wage or a wage sufficient to cover the Mexican's normal living needs, and that Article 11 of the Migrant Labor Agreement (R. 81) violates Section 501 by requiring employers to incorporate the Standard Work Contract into their employment contracts.[27/] Plainly, appellants are reading too much into Section 501(5), which is simply part of a Section delineating the Secretary's function of recruiting Mexican workers and transporting them to the areas where they are needed and has nothing to do with what measures may be taken to protect domestic workers.

The question here presented as to the Secretary's authority has not been adjudicated prior to this action. In Johnson v. Kirkland, 290 F. 2d 440 (C.A. 5), certiorari denied, 368 U.S. 889, the action was dismissed for failure to join an indispensable party. The language which appell-

27/ Limitations in the Standard Work Contract have been specifically approved in some of the legislative history relied on by appellants as authoritative. See App. Br. 47, referring to Article 10 of the Standard Work Contract (R. 100).

ants quote from the opinion (App. Br. 35) is simply a summary of the plaintiff's argument, which the court found to be "substantial" but to be "offset" by the "powerful arguments" of the Secretary. Id. at 445. The court expressly refused to rule on the merits and did not come to any conclusion either for or against appellants' contentions herein.[28/]

In short, we submit that the Secretary's action was not only authorized by Section 503(2), but indeed was required by the congressional mandate to prevent the employment of Mexican workers from adversely affecting domestic wage rates. Accordingly, if this Court deems it proper to adjudicate the question in this case, we submit that the conclusion reached by the court below must be upheld.

28/ Dona Ana County Farm and Livestock Bureau v. Goldberg, 200 F. Supp. 210 (D.D.C.), is also cited by appellants (App. Br. 35). However, if the whole case is read rather than isolated language, it will be seen to lend support to the Secretary's position, although it is by no means conclusive. There the Secretary, in an action presaging the determinations here challenged, had attacked the problem posed by the fact that prevailing domestic wage rates in the New Mexico counties where braceros were employed were substantially lower than rates for the same type of labor in the counties where braceros were not employed. The action taken was to change the criteria used in measuring the prevailing domestic rate, which was the rate at which "adverse effect" determinations were being issued under the then current administrative practice. The principal change was to include the wages of domestic workers employed on a year-round basis, although it might seem that such workers are not "similarly employed" within the meaning of Section 503(2) (Mexicans are generally employed only on a seasonal basis). The court held for the Secretary, but the opinion does not make it clear whether the basis for the holding is (1) that the method of survey was not an arbitrary method of determining the prevailing wage of domestic workers "similarly employed", or (2) that the Secretary has power to condition his adverse effect determination upon some wage level other than the prevailing rate if he believes that employment of

III. The authority delegated by Congress to the Secretary to determine the circumstances in which employment of Mexican workers would adversely affect the wages and working conditions of domestic agricultural workers similarly employed does not constitute an unlawful delegation of legislative power.

Section 503(2) provides that no braceros shall be made available for employment unless the Secretary of Labor determines and certifies that

> the employment of such workers will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed.

We have argued that the determinations here challenged are an attempt to carry out the congressional direction contained in Section 503(2) and are accordingly within the authority granted by that Section. If this argument is correct, the Secretary's discretion under Section 503(2) is confined to the taking of action for the purpose of preventing the adverse effect proscribed by the statute. We do not suggest that the Secretary has a roving license to fix a minimum wage at any level he may desire. The statute lays down a standard--adverse effect--which is considerably more definite than the standards which were held to be sufficient delimitations of delegated authority in Opp Cotton Mills v. Administrator, 312 U.S. 126, the case relied on by appellants (App. Br. 58-59).

28/cont'd.
Mexicans has adversely affected the prevailing rate. The first ground mentioned would support neither appellants' nor the Secretary's positon herein; the second ground directly supports the Secretary's position.

Indeed, on other occasions Congress has seen fit to give administrative officials authority to fix minimum wages, subject only to standards much broader than the "adverse effect" standard of Section 503(2). See 29 U.S.C. 206 (giving Secretary of Labor authority to fix certain minimum wages in Puerto Rico and the Virgin Islands); 7 U.S.C. 1131(c)(1) (giving Secretary of Agriculture authority to condition payments under the Sugar Act upon payment of wages which he finds to be "fair and reasonable"). Appellants would presumably regard these statutes, as well as many others containing similarly broad delegations, as unconstitutional. Appellants' argument goes too far, and has no support in reason or authority.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment below should be reversed and the case remanded with directions to dismiss for lack of jurisdiction. In the alternative, it is submitted that the judgment below should be affirmed.

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DECEMBER, 1963

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with these rules.

_____
Attorney

No. 18838

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

LIMONEIRA COMPANY, a California corporation, ROGER DONLON, PAUL B. KERSTEN, and E. B. ANTONELL, et al.,

Appellants

vs.

W. WILLARD WIRTZ and ROBERT C. GOODWIN,

Appellees

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF CALIFORNIA

APPELLANTS' REPLY BRIEF

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APPELLANTS' REPLY BRIEF

I. Appellees have based their arguments on matters outside the Record on Appeal.

All questions on appeal must be tried and determined by the record as certified to the Appellate Court. The record on appeal is the sole and exclusive evidence of the proceedings in the court below. The rights of the parties in an appeal proceeding must be determined on that record. 4 Am. Jur.2d 928, 929, 933; Greene v. U. S. 358 U.S. 326, 3 L.Ed.2d 340; Hooey v. Wilson 9 Wall. 501.

Therefore it was not proper for the appellees to base their arguments on appeal on alleged facts outside the record, even though some of these statements, arguments and alleged facts appear in the Congressional Record and were in fact presented to Congressional committees considering Public Law 78 and the reenactment thereof. (Appellees' Br. 5-9, 12, 20-23, 27, 30, 32, 34)

The most obvious violation of the rule against going outside the record is the inclusion of the statements made by the Secretary of Labor, the predecessor of one of the defendants in this action, in support of the actions and orders challenged in this action. (Appellees' Br. 7-10, 28) These self-serving statements and arguments of the Secretary of Labor were not presented in the trial court below under the rules of evidence, and the Secretary of Labor was not subject to cross-examination. The appellants were not given an opportunity to offer evidence in opposition to the arguments, statements and statistics presented by the Secretary. Therefore, it is highly improper for the appellees to introduce such evidence

for the first time on appeal and base their arguments thereon.

It is true that the Appellate Court may take judicial notice of certain matters not in the record of the court below, such as the acts and actions of Congress. 4 Am. Jur. 2d 934; New York Indians v. U.S., 170 U.S. 1, 614, 42 L.Ed. 927, 1165; Jones v. Merchants Natl. Bank, 76 Fed. 683. This is particularly true in the case at hand where the interpretation of an Act of Congress is involved and where the ascertainment of the Congressional intent is of vital importance.

But this does not permit the introduction by appellees of evidence such as the self-serving statements and arguments of the Secretary of Labor before Congressional committees, since such testimony has no bearing on the Congressional intent. The introduction of such material in appellees' brief and in the footnotes thereto cannot be justified on any ground.

Therefore, it is respectfully submitted that all such extraneous matter should be ordered stricken by the court and that the case be decided on the record as certified by the trial court.

Nor may the appellees properly base their arguments on appeal on the so-called wage statistics attached to the appellees' motion for summary judgment in the court below. (R. 121-155) These so-called wage statistics are referred to in appellees' brief pages 5-7, 20-22, 27, 30.

Rule 56 of the Federal Rules of Civil Procedure provides that the only evidence which may be attached to a motion for summary judgment and presented in support thereof are affidavits, and the rule sets forth specific requirements for

these affidavits. They "shall be made on personal knowledge" and "shall set forth such facts as would be admissible in evidence and "shall show affirmatively that affiant is competent to testify as to the matters stated therein". The so-called wage statistics attached to appellees' motion for summary judgment in the court below do not meet any of these requirements. They are not affidavits; it is not indicated that they are within the personal knowledge of any stated individual; and they are clearly hearsay and would not be admissible under the rules of evidence.

The requirements of Rule 56(e) as to the requirements and form of affidavits are mandatory. Sartor v. Ark. 321 U.S. 620, 88 L.Ed. 967; Bourgeois v. Chase Manhattan Bank, 139 F. Supp. 265; Roucher v. Traders, 235 F.2d 423; Zampos v. U. S. Smelting, 206 F.2d 171; Person v. U.S., 112 F.2d 1.

II. Reply to Appellees' argument that the case has not ripened into a justiciable controversy within the jurisdiction of the district court.

Appellees argue that the case before the court does not present a case, a controversy, or a justiciable issue (1) because there is no showing that the plaintiffs are about to engage in conduct contrary to the orders, (2) because there is no showing that the orders are about to enforced, and (3) because there is no substantial damage. In support of these arguments appellees have cited a number of cases.

In the case before the court the enforcement of challenged orders is direct, immediate, and automatic. Section 503(2) provides that no worker shall be available unless and

until the Secretary has made his adverse effect determination. Article 11 of the Migrant Labor Agreement provides that all employment of Mexican workers shall be governed by the terms of the Standard Work Contract. Article 13 provides that the contract must be executed at the reception center. Article 15 provides that the wage shall be the rate specified in the individual work contract, or the adverse effect rate, whichever is higher, and it provides further that the determination made by the Secretary shall be final and conclusive. Appellees admit that in order to obtain braceros in the first instance the employer must establish his eligibility and obtain the necessary authorization by complying with all of the above regulations. (Appellees' Br. 3) If he fails to do this he cannot employ braceros. If he fails to maintain his eligibility by complying with all the regulations the braceros are withdrawn. Therefore, it is sheer nonsense to argue that there is no justiciable issue because the appellants have failed to show that they are about to engage in conduct prohibited by the order or that they have failed to show that there is an immediate threat of enforcement against appellants.

Appellants have alleged (R. 4) that they are wholly or partially dependent on the use of braceros to harvest their crops. In the case of a grower who is dependent upon the use of braceros, the unavailability of braceros or their withdrawal after they have been made available could result in the loss of a crop, and it could be financially disastrous. Therefore, it is wholly unrealistic for the appellees to argue that there is

no justiciable issue because appellants have failed to show damage or threatened damage.

The case before the court comes within the purview of Columbia Broadcasting System, Inc. v. U.S., 316 U.S. 407; 86 L.Ed. 1563. This was a case in which the Columbia Broadcasting System was seeking an injunction against an order of the Federal Communications Commission. In considering whether or not there was a justiciable issue the court held:

> "The ultimate test of reviewability is not to be found in an overrefined technique, but in the need of the review to protect from the irreparable injury threatened in the exceptional case by administrative rulings which attach legal consequences to action taken in advance of other hearings and adjudications that may follow, the results of which the regulations purport to control."

This case before the court also comes within the purview of Pierce v. Society of Sisters, 268 U.S. 510; 69 L.Ed. 1071. This was an action brought by a private school to restrain the enforcement of a law to compel all children to attend public schools. At the time the action was brought the law was not to go into effect for a period of two or three years. The plaintiff alleged that by reason of the statute and the threat of enforcement the appellants' business was being destroyed and its property depreciated. The parents and guardians were refusing to make contracts for the future instruction of the children and some were being withdrawn. The court held:

> "The suits were not premature. The injury to appellees was present and very real, -- not a mere possibility in the remote future. If no relief had been possible prior to the effective date of the act, the injury would have

become irreparable. Prevention of impending injury by unlawful action is a well-recognized function of courts of equity."

In Public Utilities Com. v. U. S., 355 U.S. 534; 2 L.Ed. 470, the legislature of the State of California had amended the Public Utility Act to provide that the United States could not negotiate special rates with carriers within the state unless the Commission approved the rates. The United States filed an action for declaratory relief asking that the statute be declared unconstitutional. It was argued that there was no justiciable issue because the Public Utilities Commission had not yet refused to approve the rate negotiated by the United States. The court held:

"The controversy is present and concrete--whether the United States has the right to obtain transportation service at such rates as it may negotiate or whether it can do so only with state approval."

In Ex Parte Young, 209 U.S. 125; 52 L.Ed. 715, an action was taken by stockholders of a railroad to enjoin it from complying with a statute relating to rates. The action demanded of the corporate officers that they refuse obedience to the statute and should institute suits to prevent its enforcement. The question was presented as to whether on these facts a justiciable issue was presented, and the court held:

"It may therefore be said that when the penalties for disobedience are by fines so enormous and imprisonment so severe as to intimidate the company and its officers from resorting to the courts to test the validity of the legislation, the result is the same as if the law in terms prohibited the company from seeking judicial construction of laws which deeply affect its rights."

Applying the above enunciated principles to the case

at hand, it is submitted that none of the plaintiffs named or unnamed should be required to face the financial ruin which would inevitably result from an attempt to test the validity of the orders in question by refusing to pay the adverse effect rate fixed by the Secretary.

It is further observed that all of the cases cited by appellees involve questions regarding the unconstitutionality of the laws of Congress. The case before the court involves as its principal question the validity of an order of an administrative official acting under an Act of Congress. It is understandable that the courts are very reluctant to pass on the constitutionality of an Act of Congress and will do so only when presented with a clearly justiciable case or controversy. The same considerations which determine the existance of a justiciable issue in a case involving an Act of Congress do not prevail in a case involving an act of an administrative official. In such case it is submitted that the courts should be guided by the principle enunciated by the court in Stark v. Wickard, 321 U.S. 288; 88 L.Ed. 733:

> "The responsibility of determining the limits of statutory grants of authority in such instances is a judicial function entrusted to the courts by Congress by the statutes establishing courts and marking their jurisdiction....But under Article 3, Congress established courts to adjudicate cases and controversies as to claims of infringement of individual rights whether by unlawful action of private persons or by the exertion of unauthorized administrative power."

Appellees further argue that "general allegations of damage such as those made by plaintiffs clearly would not

be sufficient to establish damage for the purpose of jurisdictional amount under 28 U.S.C. 1331 or 1332." (Appellees' Br. 24) It might be noted in passing that the same arguments regarding the insufficiency of appellants' allegations of damage were made by appellees in a motion to dismiss, which was denied by the trial court. (R. 19 et seq.)

But by filing their motion for summary judgment in the trial court the appellees thereupon admitted the truth of all well pleaded allegations of fact in the complaint. Suckow Borax Mines Consol. v. Borax Consol., 185 F.2d 196.

Appellees seek to disprove the allegations of damage by use of the so-called "wage statistics" which were appended to appellees' motion for summary judgment in the trial court. However, as was pointed out elsewhere in this brief, these "wage statistics" are not properly a part of the record because they do not comply with Rule 56.

In any event, this is a representative action, and the so-called "wage statistics" do not apply to any of the unnamed plaintiffs in the action, and hence are not binding on them.

Regardless of the sufficiency of the allegation in question as to damage, jurisdiction in this case does not rest on the allegation of damage in the jurisdictional amount of $10,000. One basis of jurisdiction on which this case rests is 28 U.S.C.A. 1337, which requires no jurisdictional amount. Johnson v. Kirkland, 290 F.2d 440, 445, footnote 10.

Finally, it is observed that appellees' statement

that the Secretary "is anxious to have a ruling on the merits of this case" (Appellees Br. 17) must be regarded with a great deal of reserve. In every case, including the instant case, where the issue has been presented to the court for a decision the Secretary has raised defenses which have prevented a decision on the merits. Johnson v. Kirkland, 290 F.2d 440; Rio Hondo v. Johnson, 290 F.2d 471; McBride v. Johnson, 290 F.2d 475. In none of these cases would the Secretary have had reason to raise these defenses except for the purpose of preventing a decision on the merits.

III. Reply to Appellees' argument that the Secretary's determinations here challenged are attempts to carry out his statutory duty of insuring that employment of braceros does not adversely affect wages of domestic workers, and that this duty cannot be discharged merely by insuring that braceros are paid a prevailing wage which has been adversely affected by the very fact that braceros are available.

Exactly what constitutes the statutory duty of the Secretary and what authority was granted by Congress to discharge this duty are the issues before the court. The appellants in their opening brief undertook at considerable length to show what the Secretary's duties were and what powers had been conferred on him by Congress to enable him to discharge these duties. The appellants undertook to demonstrate how and by what method the language of Section 503 should be construed to show the Congressional intent. Appellants applied the canons of construction to the language of Section 503, to other parts of the statute and to other statutes dealing with the same subject matter, and to the long standing administrative interpretation of the Department of

Labor, to demonstrate that Congress intended that adverse effect be measured as against the prevailing wage. Appellants also went to great length to set forth the legislative history of Public Law 78 to show by the proceedings of Congress and the reports of the various committees in both the House and the Senate that the Congressional intent was to limit the Secretary to making determinations with respect to prevailing wage. These committee reports show very emphatically that Congress was greatly alarmed by the Secretary's action in undertaking to fix wages in agriculture.

Appellees concede: "The general principles of statutory construction expounded by appellants..are unexceptionable. We agree that the power of an administrative official is limited by the statute delegating the power, that an administrative official may not enlarge his statutory powers merely by issuing regulations, and that courts must construe statutes in accordance with the legislative intent and the plain meaning of unambiguous language." (Appellees' Br. 32)

But appellees nevertheless continue to argue, with respect to the Secretary's responsibilities under Section 503: "This duty cannot be discharged merely by insuring that braceros are paid a prevailing wage which has been adversely affected by the very fact that braceros are available." (Appellees' Br. 25)

In working toward this conclusion appellees concede that at first the administrative practice was to measure adverse effect as against prevailing wage, but then they say

(Appellees' Br. 27-28) that as administrative experience accumulated it became apparent that this was not sufficient and that the Secretary of Labor was compelled to act "to prevent subversion of the congressional mandate that domestic wages not be adversely affected by employment of Mexicans." (Appellees' Br. 28)

But this begs the question by assuming that there was any congressional mandate that the Secretary establish a minimum wage. It also begs the question by assuming that the Secretary was given the power to establish a minimum wage. How the appellees arrive at these conclusions is nowhere explained.

But as appellees proceed their argument reaches a climax with the assertion: "But despite the Secretary's plainly announced view of his own authority under Section 503(2) as it then existed, Congress in the course of extensive consideration of the Mexican labor program also failed to consider or pass any bill denying the Secretary such authority". (Appelles' Br. 29)

Here it becomes evident that appellees base their position on a new and unsupported principle of constitutional law that when an administrative official "plainly announces his view of his own authority" (Appellees' Br. 29) then it becomes encumbent on Congress to enact legislation denying him the authority he claims. Otherwise, the official may proceed with impunity exercising the power which he "plainly announced" that he possessed.

Appellees assert that the Secretary proceeded "at the direction of the President (Appellees' Br. 29) to meet his responsibilities by issuing the determinations here challenged. Certainly the Presidential statement quoted (Appellees' Br. 14) is not a Presidential mandate to assume the legislative function of fixing wages, but even if it were, the Presidency is not the depository of legislative authority.

Appellees' entire argument is based upon asserted facts which were not before the trial court, and which are not a part of the record, but which they nevertheless use to back up their assertion that the fixing of a wage was "necessary" in order to prevent adverse effect to the domestic wage level. But even assuming, for the purpose of argument, that they were entitled to rely on these facts, and assuming that the facts asserted are true, still an administrative official may not exercise authority just because he deems it necessary. Whether or not there should be a minimum wage in agriculture is a matter of policy which only the legislature has the authority to determine. An administrative official may not determine legislative policy, nor may he assume without an express grant of power from the legislature the authority to carry out what he deems to be the policy of the legislature.

Appellees brush aside everything appellants set forth regarding the legislative history of Public Law 78 and the congressional intent with respect thereto, with the observation: "Some members of Congress agreed with the Secretary...Others disagreed." (Appellees' Br. 28) As evidence of the ones who agreed, appellees cite Senator Mansfield and

Representative Bailey -- one Senator and one Congressman.

In support of their contentions appellees rely on American Trucking Assns. v. United States, 344 U.S. 298; 97 L.Ed. 337, and they state: "In the instant case Section 503(2) provides much more specific authority than was present in American Trucking, and the evil of depressed domestic farm wages is just as basic to the congressional intent as was the evil of trip-leasing practices at which the regulations in American Trucking were aimed." (Appellees' Br. 31) American Trucking does not sustain appellees' argument at all, and the differences between that case and the instant case are very clear. In American Trucking the Interstate Commerce Commission had undisputed regulatory authority over interstate trucking. This authority was not questioned. The regulations which were challenged were aimed at the practice of trip-leasing which were resorted to for the purpose of evading regulation. The rules promulgated by the Commission were for the purpose of preventing this evasion or subversion of the regulatory scheme of the Motor Carrier Act. The Supreme Court held the Commission had implied authority to promulgate regulations aimed at a practice which was used to evade or subvert the control over interstate trucking, which the Commission undeniably had. In the case before this court the Secretary of Labor is not given any control whatsoever over farm wages, or in fact over any wages, since this is strictly a legislative function. There is no reason or excuse for the Secretary to undertake to regulate farm wages other than his own asserted belief that the fixing of wages is "necessary".

Appellees argue: "Section 503(2) does not give the Secretary a roving license to fix minimum wages, even on the farms on which braceros are employed. Section 503(2) merely gives the Secretary the authority to combat a specific problem that worried Congress -- the adverse effect of braceros on domestic farm wages." (Appellees' Br. 34-35) This is tantamount to arguing that the de minimus rule applies to pregnancy.

Appellants never argued that the issue before this court was adjudicated in either Johnson v. Kirkland, 290 F.2d 440, or in Dona Ana Co. Farm & Livestock Bur. v. Goldberg, 200 F. Supp. 210; but appellants contend that the dicta in both of these cases clearly and unmistakably support their position. The quotation in appellants brief on page 35 was not a summary of plaintiffs' argument, and this is evident from the fact that this same quotation appears in Dona Ana at page 214, wherein the court points out:

> "As noted by the Court in the case of Johnson v. Kirkland, 290 F.2d 440 (5th Cir.,1961), cert. den. 368 U.S. 889, 82 S.Ct. 142, 7 L.Ed.2d 88 (1961), the interaction of elements (1), (2) and (3) of Section 503 of the Act appears to necessarily relate to the current prevailing domestic wage rate"

It is further pointed out that in the Dona Ana case, which came after the Kirkland case which is referred to therein, the Secretary of Labor agreed: "the Secretary of Labor is not authorized directly to fix wages under the Agricultural Act, but is only empowered to determine the actual prevailing wages paid to domestic workers in the area of employment which must be paid to Mexican National farm workers performing the same activity in the same area of

employment." (Dona Ana v. Goldberg supra)

The only issue decided in the Dona Ana case was that "there are no restrictions on the Secretary's power to determine what the current prevailing domestic wage rate is at any one time contained therein." (Dona Ana v. Goldberg supra)

IV. Reply to Appellees' argument that the authority delegated by Congress to the Secretary to determine the circumstances in which employment of Mexican workers would adversely affect the wages and working conditions of domestic agricultural workers similarly employed does not constitute an unlawful delegation of legislative power.

Appellants argued in their opening brief that if Congress intended to give the Secretary of Labor the authority to fix wages in agriculture, then such grant of legislative authority was an unconstitutional delegation of legislative authority. In support of their arguments appellants cited and analyzed all of the leading cases on this point, including Schechter v. United States, 295 U.S. 495, 79 L.Ed. 1570; Panama Refining Co. v. Ryan, 293 U.S. 388, 79 L.Ed. 447, and Opp Cotton Mills v. Administrator, 312 U.S. 126, 85 L.Ed. 624. In these cases the Supreme Court has set forth the principles which govern such delegation of authority, and by reference to these cases and authorities the appellants showed why the complete absence of any standards in Section 503(2) rendered the section invalid. Appellees brushed aside all of these arguments with the bland assertion: "The statute lays down a standard--adverse effect--which is considerably more definite than the standards which were held to be sufficient delimitations of delegated authority in Opp Cotton Mills v. Administrator... the case relied on by appellants." (Appellees' Br. 38)

Appellees' argument then boils down to this: That there is a delegation of legislative authority to the Secretary of Labor to fix wages and that the standard laid down for the Secretary's guidance is "adverse effect". The sole issue then before the court is whether "adverse effect" is a sufficient standard within the rule laid down by the Supreme Court in Opp Cotton Mills v. Administrator, and the other cases cited above. It is submitted that it is not a sufficient standard, particularly in view of the admission by appellees that "However, lacking any reasonable method of ascertaining exactly what domestic agricultural wages would be in the absence of braceros, the Secretary took for his standard existing state and national averages." (Appellees' Br. 31) This is an admission of the fact that there is no adequate standard set forth in Section 503(2) and that the Secretary of Labor was greatly perplexed in his effort to find one.

Since the interpretation urged by appellees would result in an unconstitutional statute, then it is submitted that the court must adopt the interpretation urged by appellants which would render the statute valid, but the orders invalid. NLRB v. Jones & Laughlin, 301 U.S. 1, 81 L.Ed. 893; Federal Trade Com. v. American Tobacco, 264 U.S. 298, 68 L.Ed. 696.

Appellees argue further: "Congress has seen fit to give administrative officials authority to fix minimum wages, subject only to standards much broader than the 'adverse effect' standard of Section 503(2)." (Appellees' Br. 39) Appellees' reference is to 29 U.S.C.A. 206, which gives the Secretary of

of Labor the authority to fix certain minimum wages in Puerto Rico and the Virgin Islands, and 7 U.S.C.A. 1131(c)(1) which gives the Secretary of Agriculture the authority to condition payments upon the payment of wages which he finds to be "fair and reasonable". However, before making these statements appellees have failed to examine fully the statutes to which they refer. 29 U.S.C.A. 205 and 29 U.S.C.A. 208 provides for the setting up of special industry committees for detailed procedures to be followed in making the so-called wage orders. Reading the entire statute, and not just the lines referred to by appellees, makes it clear that detailed standards are fixed by Congress. In the case of 7 U.S.C.A. 1131 appellees have extracted out of context just a part of the statute in question, whereas a reading of the entire section shows that the Secretary, in making the determinations as to what is fair and reasonable, is required to give due notice and an opportunity for public hearing, and he is required to take into consideration "the standards therefor formerly established by him under sections 601-608, 608a-608c, 608d-612, 613-619, 620, 623, and 624 of this title". The sections referred to and the regulations established thereunder were known to Congress at the time 1131(c)(1) was enacted, and they therefore establish the necessary standards. These statutes fully comply with the principles laid down in Schechter v. United States, Panama Refining Co. v. Ryan, and Opp Cotton Mills v. Administrator.

CONCLUSION AND SUMMARY

In conslusion, and by way of summary, appellants submit:

1. Appellees have failed to meet headon the issues raised by appellants in their opening brief. Appellees' brief is notable not so much for what they say as by what they fail to say in answer to appellants' arguments.

2. Appellees not only fail to meet head on the issues raised by appellants, but seek to sidestep the issues and avoid a discussion on the merits by arguing that there is no justiciable issue, while at the same time they assert "the Secretary is anxious to have a ruling on the merits of this case". (Appellees Br. 17)

3. The major thrust of appellees' arguments is that the challenged orders were "necessary" to enable the Secretary to carry out the congressional mandate. Appellees, however, fail to say how they conclude that there was a congressional mandate to fix wages in agriculture, or how the Secretary's notion of what is "necessary" is the proper measure of his authority.

4. Appellees' arguments of the "necessity" of an adverse effect wage are based in part on evidence outside the record and in part on the so-called "wage statistics" which are not properly a part of the record because they do not comply with Rule 56 of the Federal Rules of Civil Procedure.

5. Appellees' arguments ultimately rest on some vague and nebulous concept completely unsupported by any judicial authority that the Secretary's belief in the "necessity"

of a certain course of action is sufficient authority for him to act and that Congress's failure to enact legislation to curb "the Secretary's plainly announced view of his own authority under Section 503(2)" (Appellees' Br. 29) sustains his subsequent actions.

6. Appellees believe that the interpretation of Section 503(2) is not to be resolved by the language thereof, by the initial administrative interpretation, or by the legislative history, but rather is to be determined by reference to certain extraneous facts, such as the so-called wage statistics or statements by the Secretary of Labor and others which indicate the "necessity" for such actions.

7. Throughout their brief, and indeed throughout the whole history of their administration of Public Law 78, appellees seem to be motivated by the belief that the Secretary of Labor, and not Congress, determines the policy behind the law, and that the Secretary's power and authority thereunder is to be determined by the Secretary's conclusions as to the policy which should be pursued.

8. It is evident that appellees admit that the orders in question constitute the fixing of wages in agriculture (Appellees' Br. 38-39), but they take the position that such authority was given to the Secretary of Labor by Section 503(2) and that it is a valid grant of legislative authority under sufficient and proper standards set forth by Congress. To sustain this position appellees must necessarily come within the rules laid down by the Supreme Court in Schechter

v. United States, 295 U.S. 495, 79 L.Ed. 1570; Wichita v. Public Utilities Com., 260 U.S. 48, 67 L.Ed. 124; Panama Refining Co. v. Ryan, 293 U.S. 388, 79 L.Ed. 447; and Opp Cotton Mills v. Administrator, 312 U.S. 126, 85 L.Ed. 624. This they have failed to do.

9. Finally, the interpretation urged by appellees would necessarily result in the court declaring Section 503(2) unconstitutional because it was a delegation of legislative authority without proper standards. For this reason it is submitted that the court must adopt the interpretation urged by appellants, which would render the statute valid, but the orders invalid.

McDANIEL & McDANIEL

IVAN G. McDANIEL

LEON L. GORDON

December 1963

Attorneys for Appellants

CERTIFICATE

I certify that in connection with the preparation of this brief I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with these rules.

Ivan G. McDaniel

Leon L. Gordon

No. 18838

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

LIMONEIRA COMPANY, a California corporation, ROGER DONLON, PAUL B. KERSTEN, and E. B. ANTONELL, et al.,

Appellants

vs.

W. WILLARD WIRTZ and ROBERT C. GOODWIN,

Appellees

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA

PETITION FOR REHEARING

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ON APPEAL FROM THE UNITED STATES DISTRICT COURT
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PETITION FOR REHEARING

To the Honorable

RICHARD H. CHAMBERS, Chief Judge

WALTER L. POPE, Circuit Judge, and

GILBERT H. JERTBERG, Circuit Judge.

The appellants, LIMONEIRA COMPANY, a California corporation, ROGER DONLON, PAUL B. KERSTEN, and E. B. ANTONELL, et al., hereby petition for a rehearing to reconsider the judgment entered in this action on February 12, 1964, on the following grounds:

1. The court below erred in its decision. It held that there is no legal distinction between (1) the action of the Secretary of Labor in determining the prevailing wage and basing his adverse effect determination thereon, and (2) his action in fixing a wage for braceros and for domestic workers employed by the employers of braceros and requiring the payment of this wage as a condition to the employment of braceros.[1/] In effect the court held that there is no distinction between an administrative action of determining an existing fact, i.e., the prevailing wage, and making an administrative decision thereon, and the legislative action of fixing a minimum wage,[2/] and that the Secretary of Labor, under the authority granted him in Section 503 of Public Law 78, may in his discretion do either.

1/Opinion of trial court, p. 2, l. 6-11; p. 8, l. 1-19.

2/The government conceded that the adverse effect wage is a minimum wage fixed by the Secretary of Labor under authority properly granted by Congress in Public Law 78. Appellees' Br. p. 38-39. In view of this concession it cannot be argued that the adverse effect wage is not a minimum wage, but is only a criteria by which adverse effect is determined.

2. This decision is in direct conflict with the conclusions of the courts in Johnson v. Kirkland, 290 F.2d 440, and Dona Ana County Farm & Livestock Bur. v. Goldberg, 200 F. Supp. 210.[3/] This decision is further in direct conflict with the long established principles of constitutional law as enunciated by the Supreme Court of the United States in Opp Cotton Mills v. Administrator, 312 U.S. 126, and Schechter v. U. S. 295 U.S. 495. Even assuming that the trial court meant that the Secretary of Labor had the discretionary authority to determine the level at which the prevailing wage must be to prevent adverse effect, the decision is equally in error for all the reasons heretofore stated.

3. In their action the appellants raised some extremely important constitutional questions involving the extent of the authority of an administrative official acting under the authority of an Act of Congress. There are many parties vitally interested in the answers to these questions, and previous attempts had been made to obtain final answers to these questions in Johnson v. Kirkland, supra, Rio Hondo Harvesting Assn. v. Johnson, 290 F.2d 471, and McBride v. Johnson, 290 F.2d 475, but in each case the Secretary of Labor frustrated efforts to obtain decisions on these questions, and so the issues have remained unresolved.[4/]

4. The decision of this Honorable Court in affirming the judgment of the court below "on the basis of

---

3/The trial court seemingly cited with approval both of these cases and quoted them at considerable length.
4/In each of these cases the Secretary of Labor successfully imposed the defense of the lack of an indispensable party.

that court's opinion" leaves all of these questions unanswered and places the law in this area in a general state of confusion.

Undersigned counsel certify that this petition is not interposed for delay and that in their judgment it is well founded.

Dated March 11, 1964.

McDANIEL & McDANIEL
IVAN G. McDANIEL
LEON L. GORDON

Ivan G. McDaniel

Leon L. Gordon

ATTORNEYS FOR PETITIONERS

No. 18,839

IN THE

United States Court of Appeals

For the Ninth Circuit

ZIEGLER CHEMICAL AND MINERAL CORPORATION, a corporation of New York,
Plaintiff and Appellant,

vs.

AMERICAN GILSONITE COMPANY,
a corporation of Delaware,
One of the Defendants and Appellee.

APPELLANT'S OPENING BRIEF

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No. 18,839

IN THE

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For the Ninth Circuit

ZIEGLER CHEMICAL AND MINERAL CORPORATION, a corporation of New York,
Plaintiff and Appellant,

vs.

AMERICAN GILSONITE COMPANY,
a corporation of Delaware,
One of the Defendants and Appellee.

APPELLANT'S OPENING BRIEF

This is an appeal from the summary judgments rendered in the United States District Court for the Southern District of California, Northern Division.

The complaint (Vol. I p. 1) by plaintiff Ziegler Chemical and Mineral Corporation (hereinafter referred to as Ziegler Chemical) alleged, *inter alia,* violations of the antitrust laws of the United States through illegal conspiracies, combinations, acts in restraint of trade, interference, intimidation and harassment of plaintiff and its customers and misuse of patents by defendants.

Defendant American Gilsonite Company (hereinafter referred to as American) has counterclaimed (Vol. I p. 45) against plaintiff for $9136.00, which amount allegedly due to said American is based on settlement of disputed claims for alleged past infringement of a patent by customers of Ziegler Chemical.

Ziegler Chemical alleges in its complaint that the patent in suit is invalid.

In the counterclaim American seeks to recover $9136.00 in the first cause of action upon an alleged "account stated" and in the second cause of action upon an independent promise to pay that sum.

The District Court filed its Memorandum of Decision and Order granting said defendant's Motion for Summary Judgment on the first and second causes of action of the counterclaim on June 20, 1963 and judgment was accordingly entered on June 20, 1963. (Vol. I p. 100.)

Appellant has appealed from said judgment by filing its notice of appeal on July 18, 1963. (Vol. I p. 107.)

JURISDICTIONAL STATEMENT

Jurisdiction of the District Court was based on U. S. Code, Title 28, Section 1337 and Title 15, Section 15, said suit arising under the antitrust laws of the United States.

Jurisdiction of this Court is founded under U. S. Code, Title 28, Section 1291.

STATEMENT OF THE CASE

The issues raised by the pleadings.

Ziegler Chemical sues American and other defendants for treble damages under the antitrust acts and for declaratory judgment under the patent laws.

American filed an answer together with a counterclaim. (Vol. I p. 45.) The counterclaim alleged first and second causes of action seeking recovery of the sum of $9136.00 against Ziegler Chemical alternately upon an alleged account stated (first cause of action) and upon an independent promise to pay that sum (second cause of action).

Ziegler Chemical in its answers (Vol. I p. 62) to said causes of action of the counterclaim denied the charging allegations of both causes of action.

American moved for Summary Judgment on the first and second causes of action of its said counterclaim (Vol. I p. 66) under Federal Rules of Civil Procedure, Rules 54(b) and 56, on affidavits and exhibits attached to the affidavits.

Ziegler Chemical opposed the motion and filed affidavits in opposition with exhibits attached. (Vol. I pp. 80 et seq.)

The Court granted the Motion for Summary Judgment, upon said first and second causes of action of said counterclaim for the single sum of $9136.00 with interest at 7% per annum thereon from February 1, 1959. (Vol. I p. 100.)

Judgment was accordingly entered on June 20, 1963. (Vol. I p. 106.) There was entered also an "Order Re

Stay of Enforcement of Judgment" (Vol. I p. 105), staying enforcement of said Summary Judgment until the entering of judgment upon Ziegler Chemical's complaint, provided Ziegler Chemical file satisfactory bond. Ziegler Chemical filed such bond.

Documentary evidence.

The following constitute all the documentary evidence pertaining to said first and serond causes of action of said counterclaim:

1. Letter dated April 10, 1958 from Ziegler Chemical to American (Exhibit A of Goodner affidavit) as follows (Vol. I p. 74):

> "In line with our telephone conversation just now this is to confirm our willingness to pay you back royalties wherein we sold Gilsonite for underground pipe insulation.
>
> "I appreciate your willingness to give us a little time to do this and we will offer a payment plan for your approval shortly."

2. Letter dated April 14, 1958 from American to Esso notifying Esso that Ziegler Chemical will pay royalties on Esso installation (Vol. I p. 75), as follows:

> "At the request of the G. S. Ziegler & Company, we are writing you to state that they have agreed to pay us the royalties due on all past installations of their Tri-sul-ite. If you have such an installation, their payment to us will remove any infringement which may now exist.
>
> "They have also arranged with us for the rights under our U. S. Patent 2,668,125 to extend the

rights to practice the inventions of this patent on all future installations."

3. Letter dated December 15, 1958 (Exhibit D of counterclaim (Vol. I p. 61) and Exhibit A of Owen affidavit (Vol. I p. 79)) was sent by the sales manager of Ziegler Chemical to American reading as follows:

"At long last we have completed our work with regard to determining the back royalties due you under the above patent.

"According to our records, the total comes to $9,136.00 covering the period of 1954 to the end of February, 1958, since which time, as you know, we have been reporting and paying monthly. Our yearly tonnage figures were as below:

"1954	40 tons @ $8.00	$ 320.00
1955	28 "	224.00
1956	180 "	1,440.00
1957	773 "	6,184.00
1958	121 "	968.00
	1,142	$9,136.00

"What with all the expenses incurred this year with respect to our TRI-SUL-ITE Division, we would like to defer putting these back royalties on our books until next year, and for which reason we hope you will not mind our setting this up for payment in January of next year."

4. The report by American's auditor dated December 21, 1961 (Exhibit A of Ziegler affidavit) in part on page 9 (Vol. I p. 93) reads as follows:

"As to shipments prior to March 1, 1958, a letter from Ziegler to American indicates royalties

payable of $9,136 as of that date. After deducting the amount received of $644 indicated above, we understand that there is a balance due of $8,492. We were unable to determine whether this balance is shown on the books of Ziegler. In response to our inquiry, Mr. Ziegler said that he had discussed the balance with you about a year ago and that he had heard nothing further from you about it. We assumed from our conversation with Mr. Ziegler that his company did not expect to pay any further amounts on this balance."

5. Letter of American to Ziegler Chemical dated January 12, 1962 (Vol. I p. 95):

"Without waiving any right we may have to additional sums of money which a complete audit of your Company's books may show to be due us, we demand, and call upon you for immediate payment of, the following:

"1. The amount of $4,449.40, said sum being the deficiency revealed by the enclosed report of Lybrand, Ross Bros. & Montgomery.

"2. The amount of $9,136, said sum being the amount of the back royalties owing us in accordance with the account stated in your letter to us dated December 15, 1958.

"Again without waiving any additional rights which we may have under the license agreements between our companies, we also make demand upon you that we be permitted immediate access to such books and records as will permit our auditors to verify all of your sales of Gilsonite, both domestic and foreign, upon which royalty was owing. Please advise us promptly of the date

upon which such records will be made available for review by our auditors."

Summary of affidavits.

1. In an affidavit, E. F. Goodner (Vol. I p. 70), at one time chief executive officer of American, alleged in substance that negotiations were had with the predecessor of Ziegler Chemical between 1954 and 1958 regarding certain charges that Ziegler Chemical's predecessor sold gilsonite to users who by the use of such gilsonite allegedly infringed a U. S. patent of American; and that American allegedly obtained judgments against two such users; and that Ziegler Chemical offered to pay royalty on a particular installation and requested Goodner to assure Esso Standard Oil Co. that the latter would not be charged with patent infringement because Ziegler Chemical will pay the royalty; Goodner alleges he refused to write such letter until Ziegler signed a license agreement; nevertheless upon receipt of Ziegler's letter of April 10, 1958 (above quoted) Goodner instructed an employee to so assure Esso Standard Oil.

These Goodner allegations are contradicted in the counter-affidavit of Ziegler (Vol. I p. 80) wherein Ziegler admits that American threatened customers of Ziegler Chemical with patent infringement suits and otherwise harassed such customers between 1954 and 1958 and that in order to avoid further harassment Ziegler Chemical agreed to submit "an offer" for settlement of the controversy subject to an offset for expenses caused to Ziegler Chemical by such harass-

ment; and Ziegler Chemical alleges (and pleads in this case) that the patent under which American Gilsonite threatened customers was and is invalid, hence American had no ground for such threats.

2. American also filed an affidavit of Earl H. Owen (Vol. I p. 76) who describes himself as an officer and employee of American; alleges the ownership of the patent in suit by American; then alleges that he was *informed* by Goodner on April 14, 1958 about the execution of a license agreement between Ziegler Chemical and American for a royalty of $8 per ton. He also alleges that he was *informed* by Goodner that Mr. Gordon S. Ziegler had promised in writing to pay an amount equal to $8 per ton on all gilsonite sold by Ziegler for the practice of said patent from the date of the issuance of the patent, February 2, 1954, to the date of execution of the agreement, April 10, 1958. Then Owen confirms the instruction to inform Esso Standard Oil that "payment by Ziegler in accordance with his written promise would remove any infringement on the part of Esso arising out of the fact that they had practiced the patent in an underground pipe insulation." Owen identified Exhibit B attached to the Goodner affidavit as the letter he wrote to Esso. This letter is dated April 18, 1958. Then Owen alleges that he contacted Mr. O. G. Clement, an employee of Ziegler Chemical, regarding the accounting allegedly promised by Ziegler Chemical to compute the exact amount owing by Ziegler Chemical to American. Owen then alleges the receipt of the letter of December 15, 1958 signed by O. G. Clement, sales manager for G. S.

Ziegler Co., and alleges "American Gilsonite Company accepted this accounting as accurate and has never disputed Mr. Clement's computation set out in said letter."

3. In the counter-affidavit of Ziegler (Vol. I p. 80), Ziegler alleges with reference to the "figures" set forth in Exhibit A "that in an effort to ascertain the approximate amount which might be due to defendant American, Ziegler Chemical's sales manager made an approximate computation, the results of which are set forth in defendant's Exhibit B to affidavit of Earl H. Owen."

"That the figures set forth in said Exhibit A did not constitute an account stated but were merely tendered as an estimate with the offer that they would be 'put on the books' subject to further negotiations as to net amount due either party."

Ziegler further alleges "that the aforesaid figures were never put on the books of plaintiff."

"That defendant never acquiesced in nor agreed that said figures were correct nor alleged that said figures were an account stated until the commencement of this action."

Ziegler attached to his affidavit as Exhibit A the audit of December 22, 1961 made of Ziegler Chemical's books by American's accountants and called attention to page 9 of said audit (Vol. I p. 93), and further alleged "not only was the amount reported different than that alleged herein to be an account stated but the existence of a controversy over and lack of agree-

ment as to what, if anything, was due is clearly set forth in said Exhibit A."

4. In the counter-affidavit of Oren G. Clement (Vol. I p. 98) he also alleges that Exhibit A attached to the affidavit of E. H. Owen was a computation "to estimate the amount of back royalties which might be due, if any." Further Clement swears "that defendant at no time agreed to or acquiesced in said figures, but on the contrary ordered an audit and accounting of the books of plaintiff."

Clement further swears that "at no time did plaintiff intend" such figures as an account stated and that "because of the inability of plaintiff and defendant to agree on amount due to one from the other as the result of past transactions, no amount was ever placed on plaintiff's books to the credit of defendant."

POINTS ON WHICH APPELLANT RELIES ON THIS APPEAL

1. The Trial Court erred in granting the Summary Judgment on the First Cause of Action of the Counterclaim herein, because the pleadings herein presented genuine issues of material fact, and because the pleadings, and alleged admissions on file in this case together with the affidavits, show that there are genuine issues as to material facts and that the moving party is not entitled to a judgment as a matter of law.

2. The Trial Court erred in granting the Motion for Summary Judgment because the opposing affidavits on file considered together with the pleadings

show genuine issues of material facts, as to state of mind and intention of the parties with regard to the transactions involved; as to the purpose and nature of the audit of defendant's records; as to actual meeting of the minds of the parties with regard to the exact amount of alleged indebtedness; and as to the liability of defendants.

3. The Trial Court erred in granting the Motion for Summary Judgment on the Second Cause of Action on the Counterclaim, because the pleadings show genuine issues of fact as to an alleged promise by defendant to pay, and no affidavits were filed in support of the Motion for Summary Judgment on the Second Cause of Action of the Counterclaim; and if the affidavits in support of the Motion for Summary Judgment on the First Cause of Action are also considered in support of the Motion for Summary Judgment on the Second Cause of Action, then the Court was in error in considering such affidavits which so far that they pertain to the alleged promise by defendant are based on hearsay and not on personal knowledge by the affiant.

4. The Trial Court erred in granting of Summary Judgment on both causes of action because there are substantial questions as to the credibility of witnesses and the weight of evidence as set forth in the conflicting affidavits of the parties in this case, and it is desirable to permit the opposing party an opportunity at a trial to cross-examine the witnesses of the moving party; and the evidence in the affidavits is such that conflicting inferences could be drawn therefrom.

5. The Trial Court erred in granting the Summary Judgment in disregarding the rule that the evidence presented by the affidavits are to be liberally construed in favor of the party opposing the Motion for Summary Judgment; and that the opposing party be given the benefit of all favorable inference which might be reasonably drawn from the evidence; and that facts asserted by the party opposing the motion and supported by affidavits must be taken as true, and the rule that any doubt as to the existence of an issue of fact is to be resolved against the party moving for Summary Judgment.

6. The Trial Court erred in ruling that there is no substantial issue of fact as to the existence of account stated of the first cause of action of the counterclaim.

7. The Trial Court erred in holding that there was no genuine issue of fact as to defendant's alleged promise to pay.

ARGUMENT

The sequence of this argument shall follow the sequence of the points on which appellant relies on this appeal.

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1. THE PLEADINGS AND THE AFFIDAVITS RAISE GENUINE ISSUES OF MATERIAL FACTS.

Ziegler Chemical in its answer to the counterclaim denies the existence of an account stated or any independent promise to pay any amount, therefore issue is joined in the pleadings on these two causes of action. In this respect the instant case distinguishes

from the type of cases where liability or the existence of such an account stated or such promise to pay was admitted in the answer. Consequently no summary judgment would lie on the basis of the pleadings alone.

The affidavits in support as well as in opposition of the motion for summary judgment were heretofore analyzed in brief and are in direct conflict as to material facts.

For instance Ziegler in his affidavit swears that the letter of December 15, 1958 was merely one phase of the overall negotiations to settle the then existing claims and counterclaims between the parties. In particular Ziegler at that time contended in his negotiations with Goodner that whatever amounts may be found to be due for alleged past infringement by customers would be reduced by whatever amount it cost Ziegler Chemical to counter the harassment on the part of American in connection with the same customers. Goodner in a general way admits that there were such oral negotiations with Ziegler but in his affidavit limits the negotiations to only two customers. Ziegler Chemical is certainly entitled to a full hearing as to this phase of negotiations.

Goodner is entirely silent in his affidavit as to Ziegler's demand with regard to Ziegler Chemical's costs and expenses due to said harassment.

Goodner in his affidavit admits that Ziegler agreed only in general to "promise in writing to pay royalties" on all past sales prior to the license agreement, but Goodner, who after all during all the times at

issue was the chief executive of American does not mention at any time that Ziegler ever made a specific promise *to pay any specific amount.* It is remarkable that Goodner, who actually conducted the negotiations with the chief executive of Ziegler Chemical does not allude at all to the letter of December 15, 1958.

With regards to the affidavit of Owen, it is purely hearsay. Owen swears that Goodner, the Chief executive of American *told* Owen that Goodner and Ziegler were negotiating and that Ziegler "promised in writing to pay an amount equal to $8 per ton on all gilsonite sold by Ziegler . . . to the date of execution of the agreement on April 10, 1958." But no affidavit on either side refers to otherwise or produces any such agreement of April 10, 1958 unless Owen had in mind the subsequent license. This is ambiguous, because there is a letter of April 10, 1958 in which there is no mention made at all of "$8 per ton" or any amount. It merely confirms Ziegler's "willingness" to pay back royalties and states that Ziegler will "offer a payment plan" *for approval.* Ziegler Chemical is certainly entitled to have testimony to this effect under proper cross-examination and ascertain from Owen as to what "agreement of April 10, 1958" he has reference to and just what is the basis of the allegations in his affidavit. Also Ziegler Chemical is entitled to examine Mr. Owen as to the source of his information, if any, as to the allegations that American accepted the letter of December 15, 1958 as an accurate accounting and has never disputed the computations in that letter. After all, it is evident from the two affidavits in sup-

port of the motion for summary judgment that while Mr. Owen did contact Mr. Clement regarding this computation, neither Mr. Owen nor Mr. Clement pretended to have either the position or the authority to finalize the negotiations then in progress between the chief executive of American, Mr. Goodner and Mr. Ziegler. It is evident that Mr. Owen was an underling under Mr. Goodner and it was not his decision to accept or reject any figures or any offers from Ziegler Chemical. It is significant that there is no allegation of such acceptance of any offer in the affidavit of the chief executive of American, Mr. Goodner. At any rate there is no agreement of April 10, 1958 regarding any specific amount of back royalties to be paid to American. The letter of April 10, 1958 is a general promise and it cannot form the basis of an account stated or a promise to pay a specific amount.

One thing is clear from the Goodner and Owen affidavits and that is that Mr. Owen did what he was "instructed" to do by Mr. Goodner, and Mr. Goodner does not swear to ever accepting or approving any specific amount of indebtedness offered by Ziegler. This is a material issue of fact which should be fully litigated and not determined on vague and confusing affidavits of the type sworn to by Goodner and Owen.

The evidence before the Court was further contradictory when consideration is given to the report of the accountants of American attached to the Ziegler affidavit. On pages 8 and 9 of that report (Vol. I pp. 92, 93) American's own accountants reported on

"royalties received and receivable", which indicates an audit of December 1961 of the same items on which allegedly an agreement had been already reached. As to the balance owing on the alleged account, the accountant stated "we were unable to determine whether this balance is shown on the books of Ziegler. In response to our inquiry, Mr. Ziegler said that he had discussed the balance with you about a year ago and that he had heard nothing further from you about it. We assumed from our conversations with Mr. Ziegler that his company did not expect to pay any further amounts on this balance." Ziegler Chemical is entitled to examine the accountants or produce proof in connection with the confusion regarding this account and also to examine both Mr. Owen and Mr. Goodner as to their recollection of the substance of the negotiations alleged in the Ziegler affidavit.

All the above contradictions are material to the issues of the "account stated" and "promise to pay a specific amount" and therefore under the general rules pertaining to grounds for summary judgment the motion for summary judgment should have been denied.

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2. **THE CONSIDERATION OF THE OPPOSING AFFIDAVITS INVOLVE DETERMINATION OF THE STATE OF MIND AND INTENTION OF THE PARTIES WITH REGARD TO THE NEGOTIATIONS INVOLVED.**

There is substantial body of authority that where motive, intent, subjective feelings and reactions were to be searched, and examination and cross-examina-

tion are necessary instrument in obtaining the truth, the issues may not be disposed of on summary judgment. (3 Barron & Holtzoff Federal Practice and Procedure, 111 et seq. paragraph 1232.2.)

The affidavits in the instant case refer to the state of mind and understanding of Goodner and Ziegler, and Owen and Clement regarding the intent of their conversations and correspondence. Particularly the intent as to how the final amount, if any, owing for past infringement by Ziegler's customers should be determined.

Ziegler Chemical is entitled to introduce evidence before the Court to prove the actual tenor of the negotiations and thereby negate any implied contract or implied agreement based on a single letter which formed only one phase of the overall negotiations. Ziegler Chemical is also entitled to cross-examine both Goodner and Owen as to their recollection of the Ziegler allegations.

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3. **THE AFFIDAVITS IN SUPPORT OF THIS MOTION FOR SUMMARY JUDGMENT ON THE SECOND CAUSE OF ACTION ARE BASED ON HEARSAY AND NOT ON PERSONAL KNOWLEDGE.**

It is a basic rule of summary judgment proceedings that the affidavits must be on personal knowledge and not on hearsay. (3 Barron & Holtzoff Federal Practice and Procedure, 164 et seq. paragraph 1237.)

Even a cursory reading of the Owen affidavit which is the only affidavit that refers to any promise to pay

any specific amount, shows that Owen swears merely that he was told by Goodner as to what Goodner was told by Ziegler but he of his own knowledge does not know and was never the witness to any promise to pay any specific amount.

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4. **QUESTIONS OF CREDIBILITY OF WITNESSES AND THE WEIGHT OF EVIDENCE OUGHT NOT BE DETERMINED ON MOTION FOR SUMMARY JUDGMENT.**

"If there is any question as to the credibility of witnesses or the weight of evidence, a summary judgment should be denied." (3 Barron & Holtzoff Federal Practice and Procedure 134, par. 1234, n. 77.)

The Goodner affidavit alleges that there was a promise to pay back royalties, but does not allege that any definite amount was ever agreed upon. Owen in his affidavit alleges what he had *heard* from Goodner and then alleges the receipt of the letter of December 18, 1958 from Clement, and that American did not dispute the letter.

On the other hand Ziegler and Clement allege that the letter of December 18, 1958 was intended only as an estimate and was only a phase of the continuing negotiations and was subject to final adjustment of an amount different from that stated in the letter which was yet to have been agreed upon.

The credibility of Goodner and Clement as to the substance of the negotiations, the conduct of the parties, their conversations and the weight of the same as against any implication based on that single

letter, are vital and Ziegler Chemical is entitled to elicit the whole truth from those affiants by way of proper cross-examination.

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5. THE AFFIDAVITS WERE NOT LIBERALLY CONSTRUED IN FAVOR OF ZIEGLER CHEMICAL, OPPOSING THE MOTION FOR SUMMARY JUDGMENT.

The party opposing the motion should have been given the benefit of all favorable inferences which might reasonably be drawn from the evidence. "Facts asserted by the party opposing the motion and supported by affidavits or other evidentiary material, must be taken as true." (3 Barron & Holtzoff Federal Practice and Procedure 140, par. 1235.)

If the Ziegler and Clement allegations were to be taken as true, then the only inference that could be drawn from the evidence and affidavits would be that the total amount due to American was unliquidated and therefore there was neither an "account stated" nor an enforceable "promise" to pay any specific amount.

At any rate the Goodner and Owen affidavits if liberally construed in favor of the opposer of the motion for summary judgment, would not support a finding of either an "account stated" or a "promise" in a *liquidated amount*. Goodner merely alleges a general promise of an unliquidated amount. Owen merely alleges the receipt of the letter of December 15, 1958, and that American never disputed that letter. But this last statement of Owen is not corroborated even

by Goodner, the then chief executive of American who was admittedly in charge of the negotiations with Ziegler.

In other words the terms and nature of the agreement admittedly were to be determined by negotiations between Goodner and Ziegler. Owen and Clement, respectively "Secretary-Treasurer" and "sales manager" were merely in charge of the books to furnish some figures for the principal negotiators Goodner and Ziegler. Hence the affidavits liberally construed would support the only inference that the total settlement amount due to American was not a liquidated amount.

Additionally doubt is cast upon the contentions of American as to "account stated" and "promise" by the subsequent conduct of the parties. Namely American did not demand payment at all for three years and before demanding payment had their own accountant audit the books of Ziegler Chemical, and prior to making such demand American was advised by its own accountant of the posture of Ziegler denying any debt in such specific amount.

According to well established rules pertaining to summary judgment doubts as to the existence of such issue of facts should have been resolved in favor of Ziegler Chemical and against the motion for summary judgment.

6. THERE ARE ISSUES OF MATERIAL FACTS AS TO THE "ACCOUNT STATED" OF THE FIRST CAUSE OF ACTION OF THE COUNTERCLAIM.

An "account stated" is not merely a single unanswered communication or letter, it involves the overall conduct of the parties to establish a definite and certain intent that a liquidated amount has been agreed upon as a final settlement of claims and counterclaims then existing between the parties.

> "The action upon an account stated is not upon the original dealings and transactions of the parties . . . It is upon the new contract by and under which the parties *have adjusted their differences and reached an agreement.*"
>
> *Gardner v. Watson,* 70 Cal. 570.

As heretofore discussed in this brief the conduct of the parties in this case in 1958 and thereafter is inconsistent with a conclusion that these parties "have adjusted their differences and reached an agreement." It is evident from a review of the affidavits that these parties never adjusted their differences, hence the Court was in error is disposing of this important issue of material fact by summary judgment.

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7. THE ALLEGED "PROMISE" OF THE SECOND CAUSE OF ACTION WAS MERELY A PROMISE TO OFFER A PLAN.

The only evidence of "promise" as such is in the letter of April 10, 1958 attached to the Goodner affidavit which letter only *confirms the willingness to pay back royalties* and states that Ziegler Chemical

will offer a payment plan. The subsequent letter of December 15, 1958 furnished a tentative figure to form the basis of negotiations for a payment plan. But these parties differed right up to the present suit as to what the ultimate liquidated amount should be.

Again the conflicting affidavits, as above discussed, raise issues of material facts as to the existence of a liquidated amount on which a common count predicated on a promise to pay a liquidated amount could be based.

CONCLUSION

In general the Trial Court was in error in weighing the conflicting affidavits and in effect trying the case on its merits on such affidavits. The Court resolved disputed fact issues by reference to the affidavits contrary to well established rules of law, as summarized in 3 Barron & Holtzoff Federal Practice and Procedure 129, where in footnote 58 there is cited as an authority for such rule *Lane Bryant, Inc. v. Maternity Lane Limited, of Cal.,* C.A. 9th 1949, 173 F.2d 559, in which case at page 564 Justice Stephens stated:

> "The affidavits upon their broadest application do no more than to present to the trier of fact evidence upon material issues. They do not absolve the issues as matters of law. Therefore the judgment cannot validly be based upon the summary trial by affidavits. The plaintiff-appellant is entitled to have its complaint responded to by answer and both parties are entitled to have the issues tried through the introduction of exhibits

and witnesses produced for direct and cross-examination."

It is respectfully urged that the Trial Court was in error in granting the motion for summary judgment and that the judgment should be reversed.

Dated, San Francisco, California,
January 28, 1964.

Respectfully submitted,
GEORGE B. WHITE,
ALFONS PUISHES,
Attorneys for Appellant.

No. 18,839

United States Court of Appeals

For the Ninth Circuit

ZIEGLER CHEMICAL AND MINERAL CORPORATION, a corporation,

Plaintiff, Cross Defendant and Appellant,

vs.

AMERICAN GILSONITE COMPANY, a corporation,

Defendant, Cross Complainant and Appellee.

APPELLEE'S BRIEF

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APPELLEE'S BRIEF

JURISDICTIONAL STATEMENT

This is an appeal by plaintiff and cross defendant Ziegler Chemical and Mineral Corporation from a summary judgment for the payment of $9,136, entered in favor of defendant and cross complainant, American Gilsonite Company, on the first and second causes of action stated in American's counterclaim.[1]

---

[1]Appellant and Appellee will sometimes hereafter be referred to, respectively, as "Ziegler" and "American." "Tr." refers to the Clerk's Transcript; "O.B." refers to Appellant's Opening Brief. Inasmuch as the first and second causes of action of the counterclaim are all that is involved in this appeal, we will sometimes refer to them as "the counterclaim" collectively.

The action in which the counterclaim was asserted was commenced by Ziegler on April 12, 1962, against American and certain other defendants for injunctive relief and treble damages under the antitrust laws, and a declaration of the invalidity of American's patent (Tr. 1 ff.). With its answer, which denied all material allegations of the complaint, American filed a counterclaim, stating several claims for relief (Tr. 45-49), including the two involved in this appeal. The first and second causes of action of the counterclaim sought the same relief on alternative theories of liability and alleged, respectively, an account stated in the amount of $9,136 owing from Ziegler to American, and a promise by Ziegler, supported by valuable consideration, to pay such amount to American, and that Ziegler had not paid any part of such amount (Tr. 45-47). Those causes of action are the only causes of action involved in this appeal. Ziegler's reply to the counterclaim admitted the execution of certain documents, admitted demand and nonpayment, and generally denied the balance of the allegations (Tr. 62-65). American then moved for summary judgment on the first and second causes of action of its counterclaim. The Trial Court granted the motion and directed entry of judgment pursuant to Rule 54(b) of the Federal Rules of Civil Procedure (Tr. 100). This appeal followed.[2]

The trial court jurisdiction was based upon 15 U.S.C. 15 and 28 U.S.C. 1337. Jurisdiction of this Court is based upon 28 U.S.C. 1291 and 1294.

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[2]Enforcement of the judgment was stayed pending the conclusion of the main action on condition that Ziegler file a bond (Tr. 105).

STATEMENT OF THE CASE

Both Ziegler and American mine and sell gilsonite, a natural asphaltic substance found in the Uintah Basin in Utah and Colorado. Since 1954, American has been the owner of a patent on the use of gilsonite in insulating underground hot pipes (Tr. 13, 18). American immediately offered to license that patent to Ziegler upon substantially the same terms that Ziegler subsequently accepted in 1958 (Tr. 71). Ziegler refused to agree to those terms, but American kept its offer open, conditioned on Ziegler's agreement to pay equivalent "back royalties" on sales prior to execution of the agreement (Tr. 71). Early in 1958, American finally sued two of Ziegler's customers for patent infringement and obtained judgments in both cases (Tr. 72).[3]

While American's infringement actions were pending, Ziegler sought American's assurance that, on payment of royalties, American would not sue Ziegler's customer, Esso Standard Oil Company. American refused unless Ziegler would execute the license agreement for the future and promise to pay equivalent so-called "back royalties" on past sales (Tr. 72).

On April 10, 1958, Ziegler executed an agreement with American, obligating it to pay a royalty of $8 per ton of gilsonite to be sold for use in practicing American's patent, and allowing Ziegler to authorize its customers to practice the patent (Tr. 18-20). On the same date, Ziegler wrote a letter to American stating Ziegler's willingness to pay back royalties (Tr. 74). American promptly

---

[3]This is the same patent that Ziegler contends in the main action is invalid (Tr. 13-15).

lived up to its promise and assured Esso that Ziegler's payments would remove any infringement of American's patent (Tr. 75). On December 15, 1958, Ziegler wrote to American stating that the amount of back royalties due was $9,136 and promising payment some time during January, 1959 (Tr. 79). American accepted this account as accurate and has never disputed it (Tr. 78).

By letter of January 12, 1962, American terminated the license agreement because Ziegler had breached it in several respects (Tr. 32-34).[4]

American's counterclaim and its motion for summary judgment were based upon the two letters from Ziegler to American, the authenticity of which was admitted by Ziegler,[5] and on the affidavits of E. F. Goodner, American's former president (Tr. 70-75) and of Earl H. Owen, American's Secretary-Treasurer (Tr. 76-79). The first letter, dated April 10, 1958, stated (Tr. 74):

> "Mr. E. F. Goodner, President
> American Gilsonite Company,
> 134 West Broadway,
> Salt Lake City 1, Utah.
>
> Dear Ernie:
>
> "In line with our telephone conversation just now this is to confirm our willingness to pay you back royalties wherein we sold Gilsonite for underground pipe insulation.

---

[4]A similar agreement covering American's foreign patents which had been executed sometime after 1958 (Tr. 22-25) was terminated for the same reason at the same time.

[5]The letter of December 15, 1958, was pleaded in American's answer and counterclaim (Tr. 46, 61) and expressly admitted by Ziegler (Tr. 63). The letter of April 10, 1958, attached as an exhibit to the affidavit of Goodner (Tr. 74), was not denied in the affidavits filed in opposition to the motion for summary judgment.

"I appreciate you [sic] willingness to give us a little time to do this and we will offer a payment plan for your approval shortly.

"Yours very truly,
G. S. Ziegler and Company
Gordon
G. S. Ziegler
General Manager"

The precise amount of the back royalties Ziegler agreed to pay by that letter and his "payment plan" were contained in Ziegler's letter of December 15, 1958, to Mr. E. H. Owen, American's Secretary-Treasurer. That letter stated (Tr. 79):

"Mr. E. H. Owen, Secretary-Treasurer
American Gilsonite Company
134 Broadway
Salt Lake City 1, Utah

Re: Patent 2,668,125

Dear Mr. Owen:

"At long last we have completed our work with regard to determining the back royalties due you under the above patent.

"According to our records, the total comes to $9,136.00 covering the period 1954 to the end of February, 1958, since which time, as you know, we have been reporting and paying monthly. Our yearly tonnage figures were as below:

1954	40	tons at $8	$ 320.00
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1958	121	"	968.00
	1,142		$9,136.00

"What with all the expenses incurred this year with respect to our TRI-SUL-ITE Division, we would like to defer putting these back royalties on our books until next year, and for which reason we hope you will not mind our setting this up for payment in January of next year.

"With our best wishes for a MERRY CHRISTMAS and a HAPPY NEW YEAR, I am

"Very truly yours
G. S. ZIEGLER & COMPANY
O. G. Clement
O. G. Clement
Sales Manager"

In opposition to American's motion for summary judgment, Ziegler filed affidavits of G. S. Ziegler, plaintiff's president and general manager (Tr. 80 ff.), and O. G. Clement, plaintiff's vice president and general sales manager (Tr. 98). Neither affidavit disputed any material fact set forth in the two affidavits filed by American, and accordingly the court below granted a summary judgment in favor of American, stating in part in its memorandum of decision (Tr. 104):

"The Court finds and concludes from the record that there is no genuine issue of fact involved in the issue raised by the first and second causes of action of the counterclaim, that the record clearly shows without conflict an agreement of Ziegler to pay the so-called back royalties and that an account has been stated as to the amount due thereunder, $9,136, and that there is no just reason for delay in entry of judgment thereon."

QUESTION PRESENTED

The question presented on this appeal is whether, on the basis of the pleadings and the affidavits on file herein, the Trial Court correctly concluded that no genuine issue of fact existed with regard to American's claim for payment of $9,136, and that, as a matter of law, American was entitled to judgment in this amount.

SUMMARY OF ARGUMENT

American's affidavits together with the letters of April 10 and December 15, 1958, unquestionably establish both an account stated and a promise by Ziegler supported by valuable consideration to pay the back royalties to American. The authenticity of the letters is not disputed and Ziegler has admitted that it has not paid the amount agreed upon.

Ziegler's attempt in its affidavits to vary the express terms of the written promises cannot create any disputed question of fact because such evidence could be inadmissible as a violation of the parol evidence rule. Ziegler's state of mind and its subjective feelings and reactions are irrelevant, and appellant's arguments based thereon cannot detract from the express terms of its written promises. Likewise, the claim of invalidity of American's patent is irrelevant because such a claim, even if true, does not detract from the consideration received by Ziegler in return for its express promise to pay the back royalties.

ARGUMENT

The letters by Ziegler to American of April 10 and December 15, 1958 (Tr. 74, 79), set forth in full above, together constitute a clear, unambiguous and unconditional promise in writing to pay a sum certain, $9,136, on or before a date certain, the end of January, 1959. The second of these letters also constitutes an account stated and accepted by American.

Appellant's argument consists solely of attempts to impugn the clear and unambiguous wording of these letters and to raise factual issues not supported by the record.

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1. ZIEGLER CANNOT SHOW THAT HIS UNCONDITIONAL WRITTEN PROMISE TO PAY WAS SUBJECT TO ANY ORAL CONDITION RELATING TO AN OFFSET.

Ziegler argues (O.B. 13) that in the negotiations leading to the writing of the letters, Ziegler claimed that the amounts due American were to be reduced by claims of Ziegler for alleged harassment by American of Ziegler's customers. But the parts of the affidavits filed on behalf of Ziegler, referring to the letter of December 15, 1958, state only:

> "That the aforesaid figures were subject to an offset for expenses caused to plaintiff by defendant as the result of the foregoing harrassment [sic] of plaintiff and his customers" (Tr. 82).
>
> "That at no time did plaintiff intend these figures as an account stated since plaintiff well knew, and so informed defendant, that considerable sums were due to plaintiff from defendant growing out of the same

transactions, also as set forth in affidavit of GORDON S. ZIEGLER, herewith'' (Tr. 99).

Neither of these statements supports the argument in Appellant's brief that there was a prior or contemporaneous oral agreement that there would be any offset to the amount Ziegler promised to pay in those letters. But even if these statements could be so construed, such a claim would be in direct conflict with the clear and unambiguous wording of the written promise to pay. The Trial Court properly disregarded any attempt by Ziegler to impeach its own writing by allegations of prior or contemporaneous parol understandings. On motions for summary judgment allegations in affidavits which would not be susceptible of proof at trial must be disregarded.

Gillis v. Miners and Merchants Bank of Alaska (9 Cir. 1959) 271 F.2d 163;

Ford v. Luria Steel & Trading Corp. (8 Cir. 1951) 192 F.2d 880.

Thus, even if the affidavits filed by Appellant had set out facts showing an oral agreement or condition of offset—which they do not—such averments would be ineffective as an attempt to impeach a written unconditional promise to pay.

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2. THE CLAIM THAT CONSIDERATION FOR THE PROMISE FAILED IS WHOLLY WITHOUT MERIT. ZIEGLER RECEIVED EXACTLY WHAT HE BARGAINED FOR.

G. S. Ziegler's affidavit states that Ziegler's promise to make the payment of ''back royalties'' was conditioned on, and had for its consideration, defendant's ceasing its

alleged harassment of plaintiff's customers and that defendant did not cease such harassment (Tr. 82). As already shown, Ziegler cannot, by averments or oral side agreements or conditions, impugn the plain and unambiguous wording of its unconditioned written promise. If these averments sought to raise the defense of failure of consideration, they fail because Ziegler did not plead facts raising such an affirmative defense in its reply (Tr. 63) as required by Rule 8(c) of the Federal Rules of Civil Procedure. Thus, any such defense has been waived.

Fed. Rules Civ. Proc., Rule 12(h);

See:

Sorenson v. United States (9 Cir. 1955) 226 F.2d 460;

Kaye v. Smitherman (10 Cir. 1955) 225 F.2d 583, 594, certiorari denied (1955) 350 U.S. 913.

More important, however, the affidavits of G. S. Ziegler and Clement do not controvert the statement in Goodner's affidavit that American conditioned the execution of the license agreement of 1958 and the sending of the letter to Ziegler's customer, Esso, on Ziegler's promise to pay the "back royalties"; that Ziegler then executed the agreement and, on the same day, wrote American promising to pay the "back royalties"; and that American then sent the letter to Esso which Ziegler had requested (Tr. 72, 74, 75). Thus Ziegler received exactly what it bargained for.

These facts being undenied, the Trial Court was compelled to conclude that Ziegler's promise to pay the so-called "back royalties" was supported by valuable consideration and that no genuine issue of fact remained regarding the enforceability of Ziegler's promise.

3. THE APRIL 10 AND DECEMBER 15, 1958, LETTERS ESTABLISHED A PROMISE TO PAY A SUM CERTAIN BY A DATE CERTAIN.

Ziegler argues (O.B. 13-14, 19-20) that Goodner's affidavit does not show a promise by Ziegler to pay a specific amount. This argument is frivolous. The affidavits of Goodner and Owen must, of course, be read together. The December 15 letter stating precisely the amount of back royalties Ziegler previously promised to pay was addressed to "Mr. E. H. Owen, Secretary-Treasurer, American Gilsonite Company" (Tr. 79). Thus it was attached to Owen's affidavit. While Appellant characterizes Mr. Owen as an "underling" (O.B. 15), both the letter itself, and the affidavit of Owen, show that Owen, to Ziegler's knowledge, was then, and is now, an officer of American, namely, Secretary-Treasurer (Tr. 77).

Ziegler even claims (O.B. 14, 17-18) that the affidavit of Owen is hearsay with regard to Ziegler's promise to pay. Ziegler's promise is of course established by the written documents (Tr. 74, 79) attached to the affidavits. The conversation between Goodner and Owen (Tr. 77) related only the circumstances under which Owen, on behalf of American, wrote to Esso, Ziegler's customer (Tr. 75), to carry out Goodner's promise to Ziegler.

Thus, the Trial Court correctly considered the affidavits of Goodner and Owen, with their attached exhibits, together, and correctly found an unambiguous written promise to pay a sum certain on or before a date certain, on the basis of the letters from Ziegler to American of April 10 and December 15, 1958.

4. CLEMENT WAS AUTHORIZED TO WRITE THE LETTER OF DECEMBER 15, 1958.

Ziegler, in its brief (O.B. 14-15, 20) appears to contend that Clement was not authorized to sign the letter of December 15, 1958. The affidavits of G. S. Ziegler and Clement not only do not deny Clement's authority, but Clement's affidavit affirmatively states (Tr. 98) that he wrote the December 15, 1958, letter "at the request of plaintiff's then General Manager, Mr. Gordon S. Ziegler," and that he computed the figures contained in that letter at G. S. Ziegler's request (Tr. 80). In any event Appellant cannot now for the first time raise a spurious factual issue wholly outside the record.

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5. ZIEGLER'S LETTER OF DECEMBER 15, 1958, CONTAINING A PRECISE COMPUTATION OF BACK ROYALTIES DUE CONSTITUTES AN ACCOUNT STATED.

G. S. Ziegler's affidavit states that the letter of December 15, 1958, was only "an approximate computation" and was "merely tendered as an estimate" (Tr. 81); and Clement alleges that the letter of December 15, 1958, was never intended to be an account stated (Tr. 99).

An account stated has been defined as an

> "assent in good faith by debtor and creditor to a stated sum as an accurate computation of the amount of the matured debt or debts due the creditor * * *. A new duty arises to pay a sum so fixed" (Restatement, Contracts, sec. 422(1)).

Obviously, the debtor's secret intent that a writing, meeting on its face all requirements of an account stated,

should not have such effect is irrelevant. Even if Clement and Ziegler never heard of the concept of "an account stated" when the letter was sent, its legal effect must be judged by its contents—here an unequivocal determination of the back royalties due to American and a promise to pay the same.

That an account may be stated by the debtor as well as by the creditor is settled.

6 Corbin on Contracts (1962 Ed.) sec. 1313, pp. 268-270;

Kearney v. Bell (1911) 160 Cal. 661;

Linell v. Gordon (1920) 47 Cal.App. 691;

Cf. *Burnham v. Louis Meyers & Son* (2 Cir. 1949) 172 F.2d 84, 85.

The record establishes the prior written promise of April 10, 1958, by Ziegler to pay the so-called "back royalty" (Tr. 74). This promise is admitted by G. S. Ziegler's affidavit (Tr. 81) where he said: "plaintiff finally agreed to take a license under said patent and to pay such royalties on previous sales in amounts to be agreed upon by the parties." G. S. Ziegler's affidavit further recites that an exact determination of the royalties is difficult (Tr. 81). But the very purpose of an account stated is the striking of a balance upon a computation usually based on books of account, to which balance the parties then agree (see 6 Williston on Contracts (1938 Ed.) 5227-5228).

The letter of December 15, 1958, purported to set forth to Ziegler's satisfaction its computation, based on its own books and records (Tr. 79). That the computation is more than an "approximation" is apparent on its face. It did

not purport to round off any number but expressly stated to the exact ton the amount of gilsonite subject to royalty. The attempts of G. S. Ziegler and Clement to label this computation an approximation or estimate only (Tr. 98, 81, O.B. 22) contradict the express terms of the letter.

Finally, the letter of December 15, 1958, contains an express promise to pay the sum on or before a date certain. The contention (Tr. 81-82) that Ziegler's promise was merely to "put on the books" the amount due and that since Ziegler never put this amount on its books it does not owe it is preposterous. The promise in the letter to make the payment is clear and unambiguous.

---

6. AMERICAN AGREED TO THE ACCOUNT STATED.

Appellant does not and cannot state that American ever expressly disagreed with or disputed the account stated. Appellant merely points to the assertions of G. S. Ziegler and Clement (Tr. 82, 98) that American did not "acquiesce" in Ziegler's computation because American attempted an audit of Ziegler's records pursuant to paragraph 3 of the patent license agreement (Tr. 53, 58). The report of American's auditors is attached to G. S. Ziegler's affidavit and speaks for itself. This report expressly states (Tr. 85) that American's instruction to its accountants was to audit *only royalty payments due under the written license agreement* of February 18, 1958 (executed by Ziegler on April 10, 1958), i.e., royalties due after the date of the license agreement. Thus, the back royalties stated in the December 15th letter were clearly outside the scope of the audit, and no inference can be drawn from that audit that American disputed the December

15th computation. On the other hand, the fact that American limited its audit to royalties due after the agreement was executed confirms the fact that it was satisfied with the computation set forth in Ziegler's December 15th letter.[6]

Similarly, the access to Ziegler's books and records demanded by American's letter of January 12, 1962, clearly related only to the audit under the license agreement which had been frustrated by Ziegler's refusal to make its records available (Tr. 95-97). In fact, this letter constitutes an express acceptance of the account stated, since it demands payment of

> "The amount of $9,136, said sum being the amount of the back royalties owing us in accordance with the account stated in your letter to us dated December 15, 1958" (Tr. 96).

Thus, the record shows without contradiction that American expressly assented to the account stated in Ziegler's letter of December 15, 1958. Ziegler states no facts from which a failure by American to acquiesce could be inferred.[7] On the facts revealed by the record,

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[6]Ziegler contends (O.B. 9-10, Tr. 82) with respect to the accountant's report that the amount reported therein is different from the amount alleged herein to be an account stated. This refers to the mention in the report of a $644 payment prior to March 1, 1958 (Tr. 93). That the accountants were in error in deducting this payment is confirmed by Ziegler's reply to the counterclaim, which expressly admits that no part of American's claim for $9,136 has been paid (Tr. 46, 47, 63). Furthermore the audit shows on its face that payments or obligations not arising out of the two written license agreements were not within the scope of the audit ordered by American.

[7]The claim that American did not demand payment for three years (O.B. 20) is not supported by the record, and in any event, an absence of an earlier demand is immaterial.

American's failure to object would in law have amounted to an acceptance long prior to American's letter of January 12, 1962. If American now disputed the correctness of Ziegler's computation of December 15, 1958, Ziegler could properly point out that American's failure to challenge the computation within a reasonable time constituted assent and barred American from challenging the correctness of the account.

See:

6 Corbin on Contracts (1962 Ed.) p. 270;

Restatement of Contracts, sec. 422(2);

Oil Co. v. Van Etten (1882) 17 Otto (107 U.S.) 325, 333-334 (holding a lapse of four to five months unreasonable);

Reed Research v. Schumer Company (D.C.Cir. 1957) 243 F.2d 602, 604;

Willard Helburn, Inc. v. Spiewak (2 Cir. 1950) 180 F.2d 480, 483.

Since assent implied from acquiescence results in the creation of a new obligation on the account stated, Ziegler, as well as American, was bound by the computation contained in the letter of December 15, 1958, when American retained the letter without protest for a reasonable period of time. This reasonable period would have expired long before the audit which took place late in 1961 and long before this action was commenced.

CONCLUSION

For the foregoing reasons we submit that the judgment of the court below on appellee's counterclaim must be affirmed.

Dated: San Francisco, California,
March 2, 1964.

Respectfully submitted,
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Of Counsel.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

THOMAS E. HAVEN,
Attorney for Appellee.

No. 18,839

IN THE

United States Court of Appeals

For the Ninth Circuit

ZIEGLER CHEMICAL AND MINERAL CORPORATION, a corporation of New York,
Plaintiff and Appellant,

vs.

AMERICAN GILSONITE COMPANY,
a corporation of Delaware,
One of the Defendants and Appellee.

APPELLANT'S REPLY BRIEF

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No. 18,839

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ZIEGLER CHEMICAL AND MINERAL CORPORATION, a corporation of New York,
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One of the Defendants and Appellee.

APPELLANT'S REPLY BRIEF

Appellee's brief omits certain salient facts and disregards rules of law applicable to account stated.[1]

For instance, Appellee's Statement of the case does not mention that the alleged antecedent debt was an unliquidated contingent liability of Ziegler's *customers.* Ziegler was selling gilsonite, which is a mineral not covered by any patent. (Tr. 4, Par. 12.) Gilsonite could have been used by Ziegler's customers in

[1]Appellant and Appellee will sometimes hereafter be referred to, respectively, as "Ziegler" and "American". "Tr." refers to the Clerk's Transcript; "O.B." refers to Appellant's Opening Brief; "A.B." refers to Appellee's Brief.

other ways and for other purposes than those described in the patent of American.

Consequently, when Ziegler, in order to avoid harassment of his customers, offered to pay a royalty on behalf of his customers for each ton used by such customers in a certain way, Ziegler assumed an unliquidated obligation on behalf of third parties, namely its customers and in a disputed amount to be agreed upon by the parties. (Tr. p. 81.)

The letter of American to Ziegler of January 12, 1962 (three years subsequent to the offer of Ziegler), demands payment of back royalties, but this demand is made without waiving any right to additional sums which a complete audit may show to be due. This is an important fact indicating that the accurate amount allegedly due was even on January 12, 1962, still unliquidated.

American's statement (A.B. 6) that the Ziegler and Clement affidavits did not dispute any material fact set forth in the affidavits filed by American is effectively answered in the "Summary of Affidavits" pages 7 to 10 of Appellant's Opening Brief.

THE LETTERS OF ZIEGLER OF APRIL 10 AND DECEMBER 15, 1958 (Tr. 74, 79), CONSTITUTE MERELY AN OFFER OF SETTLEMENT OF AN UNLIQUIDATED CLAIM AGAINST ZIEGLER'S CUSTOMERS.

Almost the entire argument of appellee is based on the assumption that Ziegler's letters of April 10 and December 15, 1958, constitute an "account stated",

and no parol evidence would be admissible as to the circumstances surrounding the writing of these letters and as to the negotiations leading to the same.

The authorities cited on page 9 of American's Brief pertain to parol evidence in the case of the assignment of a building contract or in the case of written purchase agreements. Even under such circumstances in the case of *Ford v. Luria Steel and Trading Company*, 192 F. 2d 880, 882, cited by American, the Court of Appeals disagreed with the reasoning of the Lower Court that parol evidence tending to show "oral profit sharing agreement" was substantially inconsistent with subsequent actions of the parties, hence defendant there could not have prevailed. The Court of Appeals stated:

> "We question the validity of the second reason given by the District Court for its action. A surmise or belief, no matter how reasonably entertained, that a party cannot prevail upon a trial, will not justify refusing him his day in court with regard to material issues which are not clearly shown to be sham, frivolous, or so unsubstantial that it would obviously be futile to try them."

This is particularly important in the case of an alleged "account stated". A perusal of the affidavits and the exhibits in the case at bar shows that the consideration, if any, for the alleged account stated was the discharge of an unliquidated liability of third parties, hence parol evidence regarding the respective claims and counterclaims of the parties is relevant and admissible.

If, arguendo, the letters of Ziegler were considered as admissions, even then all the facts should be considered as to whether or not such admission is of the kind which could give rights on an "account stated".

6 Williston on Contracts (1938 Ed.) 5233, states the rule:

> "It should be remembered it is necessary to establish not an admission as such, but an implied promise; and all the facts of each case should be admissible in order to determine whether such an implication is warranted."

Consequently, Ziegler is entitled to introduce evidence to any and all contemporaneous understanding alleged in the affidavits.

> "An action on an account stated raises primarily a question whether both parties intended the transaction to become a full and final settlement of the indebtedness represented by the account. That question is usually one of fact to be determined by the jury or trial court from all the circumstances."
>
> 1 Cal. Jur. 2d, page 411.

CONSIDERATION FOR THE IMPLIED PROMISE IS AN ESSENTIAL PART OF ESTABLISHING AN "ACCOUNT STATED".

It is stated in 6 Williston on Contracts (1938 Ed.) on page 5236:

> ". . . and now an account stated is open to a wide variety of attack. Of course, it may be shown that the parties never agreed to an account stated. . . . But it may also be shown not only that the

> transaction was without consideration because the promise of the debtor was supported by no previous debt. . . . but that the consideration was illegal, or that there was failure of consideration or mistake."

The burden is on American to prove the alleged "account stated" and that it was supported by a previous debt of Ziegler to American. Such proof may be rebutted by Ziegler by showing that there was no previous debt owing by Ziegler to American, and further that Ziegler mistakenly believed that American could proceed against his customers for patent infringement on a valid patent, and also that the customers of Ziegler had liability to pay some royalty to American contingent upon the manner in which they used the gilsonite.

THE ARGUMENTS ON PAGES 11 TO 16 INCLUSIVE IN APPELLEE'S BRIEF ARE UNTENABLE IN FACT AND IN LAW.

The argument of American with regard to the Goodner and Owen affidavits on page 11 of Appellee's Brief demonstrates that there are material facts at issue, for instance as to the authority of Owen to bind American to a settlement of an unliquidated claim; as well as the actual subject of the conversation between Goodner and Owen throwing light upon the circumstances surrounding the threats of American against Ziegler's customers; and also the actual verbal understanding between the principal and negotiators, Goodner and Ziegler.

The argument on pages 12 and 13 of Appellee's Brief that when an account is stated by the debtor no "assent" by the creditor is required is refuted by American's cited authority. It is stated in 6 Corbin on Contracts (1962 Ed.) pp. 268-269:

> "Here, again, if the debtor's accounting is an offer to compromise and settle a claim then understood to be doubtful or disputed, the creditor's assent is necessary. Without it, there is only an unaccepted offer, one that is conditional on acceptance just as in the case of other offers."

In the case at bar, the alleged claim of American against the customers of Ziegler was doubtful and disputed. In fact it was disputed right up to the filing of this action and is still in dispute.

The above text continues on page 269 as follows:

> "Even though the statement of account is rendered by the debtor, with an enforceable promise to pay the amount, it is not customary to call it an account stated unless the creditor expresses his assent to it."

As it is stated in 1 Cal. Jur. 2d, page 380:

> "The rendering of an account, however, is only a circumstance which with others may or may not establish an account stated."

Consequently, the argument that the letter of December 15, 1958, constitutes an "account stated" or a promise to pay, is not consistent with the circumstances surrounding the transaction, nor with the law pertaining to it.

The argument of plaintiffs on pages 14 to 16 inclusive that American agreed to the "account stated" is contrary to the facts and the law of the case at bar.

American omits the introductory part of its letter of January 12, 1962, preceding the portion quoted on page 15 of its brief, namely that the demand was made without waiving any right to a complete audit of Ziegler's books for additional sums of money that may be due.

Consequently, even if, arguendo, American's letter of January 12, 1962, may be deemed "acceptance", it is a conditional acceptance subject to further audit.

American argues primarily that assent should be implied from its long silence.

The authorities cited on page 16 of American's brief pertain to liquidated claims or to long course of dealings between the parties. But 6 Corbin on Contracts (1962 Ed.), page 285, expressly distinguishes unliquidated and undisputed items from accounts based on merely addition and subtraction of numerical items, stating:

> "As previously indicated, however, it is necessary to consider separately the kind of an account that is merely the addition and subtraction of numerical items and a very different kind that introduces a compromise of disputed items or an agreed determination of previously unliquidated ones. If an 'account stated' is of the latter kind, the law applicable to it is the law of compromise and the law of accord and satisfaction. In these cases, it is misleading to deal with the matter under the general heading of 'account stated' ".

Also 6 Corbin on Contracts (1962 Ed.) page 267, states the rule:

> "If either the creditor or the debtor offers to liquidate a claim theretofore uncertain in amount or to compromise a doubtful or disputed claim by the payment of a specified amount, it is without question that an assent by the offeree is necessary. Such an offer is not even an admission as to an amount due. In cases of this sort, it is not often that silence should be interpreted as an expression of assent; in rare cases the surrounding circumstances may justify such an interpretation."

The case at bar evidently is not such a "rare case" because the circumstances surrounding the transaction are quite involved and the compromise is still in dispute.

American refers on page 16 of its brief to the creation of a "new obligation" on the account stated between the parties, but disregards the rule that the antecedent indebtedness, the discharge of which is the consideration for "new obligation" on an "account stated", must be between the parties to this account stated and not with a third party. Apart from any other argument, it is clearly evident from the affidavits that the unliquidated antecedent indebtedness in the case at bar was between American and third parties, namely the customers of Ziegler.

Swim v. Juhl, 72 Cal. App. 363;

Anderson v. Johnson, 101 Cal. 2d 418, 422.

CONCLUSION

It is respectfully urged that the judgment of the Court below on the counterclaims should be reversed.

Dated, San Francisco, California,
March 18, 1964.

Respectfully submitted,
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